Economics for Consumers

SECOND EDITION

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ECONOMICS FOR CONSUMERS, 2d Ed.
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To

AVERY A. SHAW

President Emeritus
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Preface

A curious anomaly in economics is that most textbooks treat the subject almost entirely from the point of view of production and producers. This in spite of the fact, pointed out by Adam Smith,[1] that

"Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer.

"The maxim is so perfectly self-evident, that it would be absurd to attempt to prove it."

Yet now, as then under the mercantile system,

". . . the interest of the consumer is almost constantly sacrificed to that of the producer; and it [the system] seems to consider production, and not consumption, as the ultimate end and object of all industry and commerce."

As the title of this book indicates, this study of economics is approached from the consumer viewpoint. The usual treatment of economics seeks to explain how goods and services are produced and how they are distributed among groups and individuals. Where the customary course in economics stops is where *Economics for Consumers* begins. Students who have had no previous training in economics may study it with benefit, learning some of the principles fundamental to economics, while those who have studied economic principles may pursue their analysis from a new angle. For example, the traditional treatment of value may be supplemented by using chapters 4–14 in Part Two.

The distinctive feature of *Economics for Consumers* is that it works through established economic principles, always from the consumer point of view. The dominant fact is the prevalence of waste in current consuming practices. The central theme is consumer welfare. The main objective is to discover and point the way toward wiser consuming practices calculated to promote human welfare. The subject matter is necessarily controversial, but the treatment of it aims at objectivity. Displacement of emotion by reason is the first sure step toward wiser consumption.

[1] SMITH, Adam. *An Inquiry into the Nature and Causes of the Wealth of Nations*, Vol. II, Bk. IV, Chap. VIII, pp. 130, 131, in Eleventh London Edition by William Playfair. Hartford: Printed for Oliver D. Cooke, 1811.

There is no science of consumption in the sense that consumer reactions can be reduced to laws and predicted in advance. Consumption is an art, which Americans have too long neglected. It is the task of future generations to match the productive genius of their ancestors with cultivation of the art of living. This will require active, alert participation in economic life comparable to that exercised by producers. Where waste prevails it must be eliminated. False standards of consumption must be replaced. The whole emphasis must be shifted from that which regards consumers as a mere source of profit to one which holds promotion of their welfare as the supreme purpose of the economic system.

It has been difficult at times to decide what should be included and what should be excluded. Whole chapters on buying shelter and insurance have been included, while the buying of food and clothing is given only brief attention along with other subjects, not because they are considered less important but because experts in home economics can treat those subjects far more effectively; and also because the main purpose of this book is to present principles as a guide to action rather than factual information and rules of buying procedure.

In the following pages the word "producers" is used in a broad sense to include manufacturers, handlers, dealers, etc., while the word "sellers" includes retail and wholesale sellers of goods and services, including advertisers.

The Questions for Discussion at the end of each chapter are drawn from my classroom experience. No effort has been made to include a question on every point; rather the purpose is to tie together the subject matter of the chapter with the students' experience and observation, and with principles of economics, and to show the relation of the subject matter in one chapter to that in another.

Likewise the Problems and Projects are ones which have been used successfully in my conduct of the course. The project is a helpful laboratory device which gets the students into the market place where they may test themselves and their buying practices against the standards suggested in the text. The shorter problems, used in connection with each chapter, give the members of a class opportunity to share their experience and observation on particular phases of each topic. Over a period of time one can collect significant source material.

Economics for Consumers is an outgrowth of a course by that name which has been offered at Denison University since 1932. Scores of Denisonians, particularly those who studied with me in the early years of the course, have contributed to the development of this book. This was made possible by using the text in preliminary mimeographed form for several years. One of my former students, Elizabeth Thomas Owen,

has worked with me on the manuscript from its inception to its completion. My obligations to her are very great.

My colleagues in other places have been very helpful. Those portions of the mimeographed edition dealing with their special fields of knowledge have been read by Professor Henry Harap of George Peabody Teachers College; Professor Paul F. Gemmill, University of Pennsylvania; Dr. LeBaron R. Foster, Pollak Foundation for Economic Research; Mr. George P. Larrick, Chief Inspector, Food and Drug Administration; Mr. E. R. Bowen, Executive Secretary, and Mr. Wallace J. Campbell, Assistant Secretary of the Cooperative League of the United States of America; Mr. Carl R. Hutchinson, Educational Director, Ohio Farm Bureau; and Mr. Roy Edwards of the Sun Life Assurance Company of Canada. It goes without saying, however, that I alone am responsible for all statements of fact and expressions of opinion, unless they are expressly quoted or paraphrased.

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Preface to the Second Edition

Much has happened in the field of consumer economics since *Economics for Consumers* was published in May, 1939. Since that time the United States has passed from a peace to a defense economy and, at this writing, is in a war economy. Some of the consumer problems created by these rapid changes are discussed in a new Part Four, entitled "Consumers in a Changing Economy," which deals with some of the problems of "Adjusting to New Controls" (Chapter 29).

Soon after completing the first edition of *Economics for Consumers* I undertook a long-range research program dealing with governmental aids to consumers. That work still goes on but some of its results are included in this edition. As Research Specialist for the Consumer Division of the Advisory Commission to the Council of National Defense I discovered the chaotic situation with reference to weights and measures. As a result, a new chapter—number 26—has been added, which deals with the important problem of weights and measures.

Since 1939 there have been some significant additions to the literature of consumer economics. The Twentieth Century Fund's answer to

the question, "Does Distribution Cost Too Much?" was published shortly after the first edition of *Economics for Consumers*. The Harvard study conducted by Professor Neil H. Borden on "The Economic Effects of Advertising" appeared in 1942. Detailed and final findings of the Consumer Purchases Study are now available and have been used in the present edition. The Temporary National Economic Committee has made available a series of monographs, among which those on Consumer Standards, Consumer Problems, Insurance, and Competition and Monopoly have proved fruitful sources of information. Finally, the results of the 1940 Census have been made available and have been used at various points in the present edition.

In this second edition also it has been possible to evaluate the Federal Food, Drug, and Cosmetic Act in operation, as well as Federal Trade Commission control of advertising. The Wool Products Labeling Act was passed in 1939 and has since gone fully into operation. Account has been taken of the extensive reorganizations in the Federal government affecting consumers, such as the shift of the Food and Drug Administration to the Federal Security Agency, the demise of the Consumers' Counsel Division in the Department of Agriculture, and the rise and decline of the Consumer Division of the Office of Price Administration.

Recent developments in advertising, price comparisons, installment buying, consumer education, consumer co-operatives, and insurance have been included in this edition.

The published *Proceedings* of the three National Conferences on Consumer Education under the auspices of the Institute for Consumer Education, are an important contribution to the literature of consumer economics.

For critical reading of various chapters and suggestions for their improvement, I am indebted to Dr. William Trufant Foster, Pollak Foundation for Economic Research; to Mr. Wallace J. Campbell, Director of Information, The Cooperative League of the United States of America; to Professor Ralph H. Blanchard, Columbia University; to Dr. Oscar A. Olson, McPherson College; to Mr. Luther W. Hemmons, Jr., Office of Price Administration; to Lieutenant (j.g.) Reign S. Hadsell, formerly of the Consumers' Counsel Division; to George P. Larrick of the Food and Drug Administration; to Professor Colston Warne, Amherst College; and to Ensign John G. Turnbull, a Denison colleague.

In addition to published sources of information, many people have responded to my direct request for factual information. Among these I wish to express my appreciation to Mr. Alfred G. Howe, Manager, The People's Consumer Co-Operative, Chicago; to Dr. David McCahan, Dean, The American College of Life Underwriters, Philadelphia; to

Mr. Clyde Casady, Executive Secretary, Savings Bank Life Insurance Council, Boston; to Mr. David L. Shultes, Insurance Department, State of New York; to Mr. Morvin Duel, Commissioner of Insurance, State of Wisconsin; to Mr. Harold W. Breining, Assistant Administrator, Veterans Administration; to Mr. Ephraim Freedman and to Mr. Q. Forrest Walker of R. H. Macy & Co.; to Mr. H. W. Riehl of the Better Business Bureau of St. Louis, and to Mr. Homer E. Frye of the Columbus Better Business Bureau; to Mr. Ralph W. Smith of the National Bureau of Standards; and to Mrs. Frances F. Garmon, Bureau of Consumers' Service, Department of Markets, New York City.

Colleagues in other institutions who have used the first edition and who have given me helpful suggestions for the second edition include Professors Marian Breck, University of Cincinnati; Hartley Cross, Connecticut College; Edwin L. Clarke, Rollins College; Z. C. Dickinson, University of Michigan; F. J. Turille, The Kansas State Teachers' College; Harold W. Guest, Baker University; W. Lou Tandy, Western Maryland College; and Hazel Van Ness, The Stout Institute.

Specific acknowledgment has been given in the footnotes to authors and publishers whose material has been used, but I wish to include this statement of appreciation for their permission to incorporate copyrighted material.

In preparing the manuscript for publication my work has been lightened by the use of Denison University facilities. Chief among these has been the William Howard Doane Library. My obligations are especially great to Mrs. George Grogan, Mrs. Walter Secor, and Miss Pauline Hoover. Denison students have continued to improve *Economics for Consumers* with their suggestions. Among that group Thelma Willett, June Pyne, George Muench, and John Donovan have been especially helpful in gathering information, typing the manuscript, and proofreading.

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1

The Functions and Responsibilities of Consumers

The Nature of Our Economic System

What Makes Our Economy Go? The purpose of a good economic system is to provide an abundance of goods and services efficiently and to distribute them widely among consumers. In other words, the main purpose of economic effort is, or should be, to satisfy as many consumer wants as possible. It is important always to keep this central, fundamental purpose in mind. There is a very great tendency to become so absorbed with particular aspects of the economic system that one loses sight of its enduring, fundamental purpose. Some of those who wander into bypaths of economic thinking gain the impression that the primary purpose of our economic system is to provide profit for owners of enterprise, or to provide jobs for workers, or to provide tax revenue for government. All of those purposes are necessary and desirable, but they are still incidental to the fundamental purpose of satisfying human wants.

Men and women and children must have food and clothing and shelter to satisfy their minimum needs and wants. There are many other kinds of economic goods they wish to have and many kinds of services they wish to enjoy. In order to provide as many as possible of those goods and services, approximately 53,000,000 men, women, and youths in the United States were gainfully occupied in 1940. Engaging in hundreds of different kinds of occupations, most of those men and women worked from 40 to 48 or more hours each week making their small contributions toward the production of economic goods which it was assumed consumers would buy when offered on the market. Those contributions took the form of adding some kind of utility to tangible goods or the performance of services in connection with the productive

process or directly for consumers. For example, all those associated with the coal-mining industry were concerned with getting coal to the surface, cleaning it, and grading it for consumers. It is customary to speak of such services as creating form and place utility. Then workers associated with rail and truck transportation began to haul the coal to various markets where consumers might purchase it; it is customary to speak of those types of services as creating place utility. Then people connected with the marketing aspect made it possible for consumers to purchase the coal and arranged to have it delivered to individual homes; those types of services are usually described as helping to create place, time, and possession utilities. People associated with the hardware and supply business had already provided consumers with furnaces or stoves, and workers who keep them in good operating condition are performing direct personal services to owners wanting that help. Notice that the entire end purpose of this whole process is to get coal into the home of the consumer where it will satisfy his wants by providing a source of heat. Notice also that although the 53,000,000 people engaged each week in performing services of that type spend 40 to 48 hours or more in productive activity, they are also consumers every moment of the 168 hours in each week. While they are at work they are consuming clothing, shelter, and food. When their working period ceases doubtless their consuming activities take on greater variety. In view of the fact that all people are consumers 168 hours every week, whereas only a portion of them are producers for only parts of the week, it is evident that the study of economics should deal at length with the consumer aspect of economic activity.

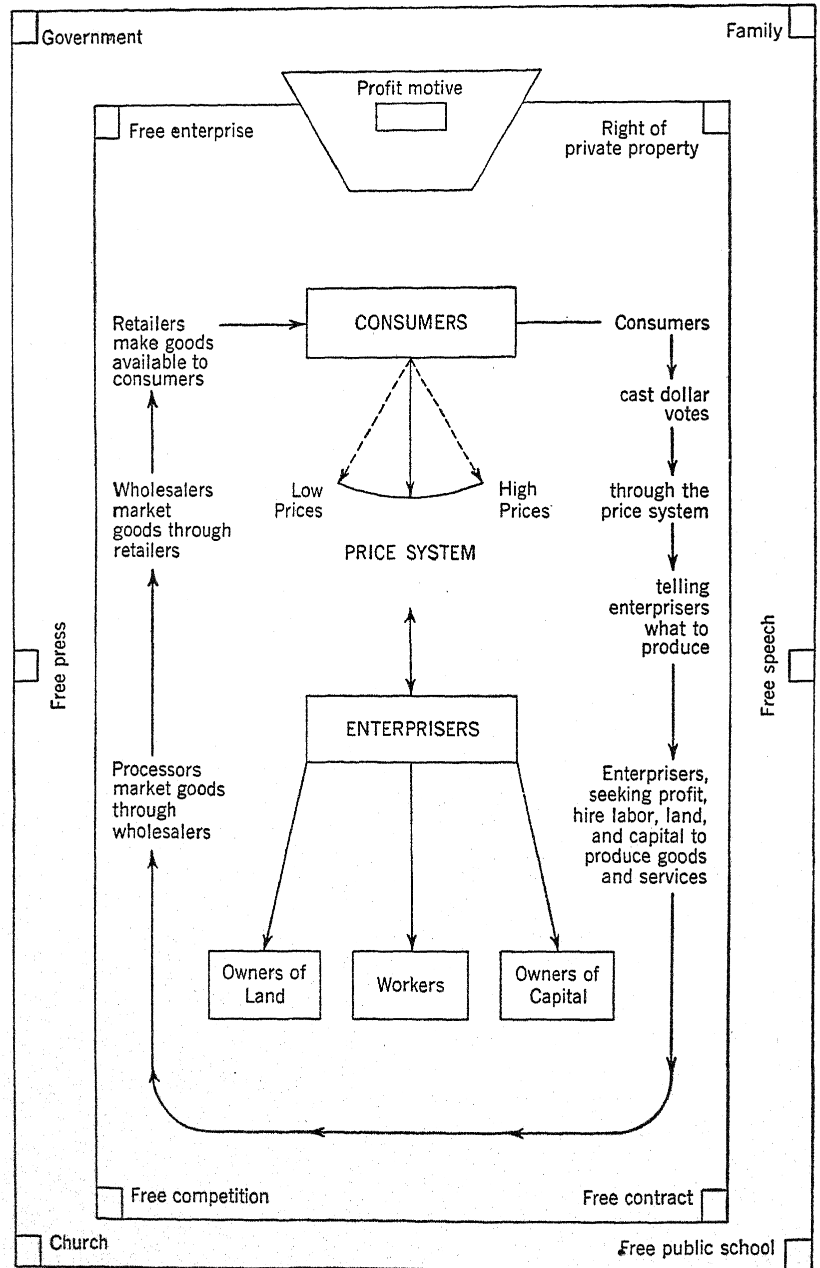
There are about 23,000,000 additional workers in American homes who are not listed as gainfully occupied, but who are among the most important in the productive activities of our economy. The 23,000,000 women who are listed as housewives operate miniature hotels in which they provide food and shelter for the members of their families. If all 23,000,000 women were to give up their jobs as housewives, it would be necessary to rehire them or others to do the same work and they would then be gainfully occupied. The fact that they do not receive money wages does not alter the fundamental fact that they are engaged quite as fully in productive economic activity as the 53,000,000 who work mostly outside the homes. The productive activities of housewives take the form not only of cooking, sewing, serving meals, washing dishes, and so on, but also the creation of form utilities in baking bread, canning vegetables, and making jellies. Many housewives operate miniature laundries in their own homes, doing their own washing, ironing, cleaning, and pressing. As the managers of these 23,000,000 establishments,

housewives become also the most important consumers in the economy. This is not because they consume more than other members of the family, but rather because they exercise much more influence in deciding what shall and what shall not be purchased for family consumption. Not only do they make nearly all decisions concerning the purchase of food, but they exercise considerable influence in the choice of household appliances and furniture, clothing for other members of the family, the choice of a house, and even the choice of an automobile. Like the 53,000,000 who work outside the homes, these 23,000,000 who work within the homes are producers part of the time, but consumers all of the time.

In addition to the 53,000,000 workers outside the homes and the 23,000,000 housewives, there remain about 60,000,000 men, women, and children in the United States who are not engaged in productive enterprise, but none the less consume 168 hours every week. Some of these are older people who are living on incomes from savings made during the days of their productive effort. Others are children who have not yet reached the age where it is desirable for them to undertake gainful occupations. Still others are men, women, and children who are incapacitated and for whom others in the economy must assume the responsibility of providing the necessary food, clothing, shelter, and other goods and services to satisfy their wants.

Who Decides What Shall Be Produced? Many of us who have been reared within the economy in which we live have (quite understandably) never given any thought to the question How is it decided what shall be produced? We are accustomed to finding in the market place practically anything we want, but we are not accustomed to giving thought to how those goods and services come to be provided. In the case of an army camp in which there are thousands of soldiers, no one is particularly surprised to find that food, clothing, and shelter in approximately the correct and necessary amounts have been provided. The system by which this is accomplished is fundamentally different from that by which the consumers of a large city are provided with the things they want. In the case of the army, the soldiers have practically no freedom of choice. Supply officers decide what kind of shelter shall be provided, what kind of food shall be served, what kind of clothing shall be issued. The men take it, whether they like it or not. By contrast, in a large city day after day consumers find in the markets approximately the right amounts of food, clothing, and shelter. Who are the supply officers for this civilian army of consumers? Most of them are self-appointed enterprisers.

This means, for example, that some man who has to make a living decides that he prefers to do so by going into the retail grocery business. Under our system of free enterprise, he is free to make that choice. If


Government
Family
Profit motive
Free enterprise
Right of private property
Retailers make goods available to consumers
CONSUMERS
Consumers
cast dollar votes
through the price system
telling enterprisers what to produce
Wholesalers market goods through retailers
Low Prices
High Prices
PRICE SYSTEM
Free press
Free speech
ENTERPRISERS
Processors market goods through wholesalers
Enterprisers, seeking profit, hire labor, land, and capital to produce goods and services
Owners of Land
Workers
Owners of Capital
Free competition
Free contract
Church
Free public school

he calculates correctly, a portion of the purchases made by consumers will be made in his store and soon he will come to know approximately what quantities of each type of product to keep on hand from day to day. In other words, he estimates what his consumer customers will purchase daily, weekly, monthly, and yearly. Those decisions are passed on to his wholesale suppliers in the form of orders, and the wholesale suppliers pass them on to the processors and the extractors of raw materials in the form of orders. Notice this important fact: the civilian consumer is perfectly free to change his mind at any time concerning his economic choices. Although the retail grocer may have ordered bread and butter and milk on the assumption that all of his customers will buy their usual amounts that day, any one of the customers is free at any moment to change his mind and fail to take his usual quota. This privilege of choosing freely what we shall and shall not consume is a very important freedom and carries with it very great responsibilities.

How Does the Price System Operate? The central co-ordinating force through which consumer demands are registered for the benefit of those engaged in the business of satisfying consumer demand is the price system. Free to make their choices, consumers register the results of their decisions in the market place by purchasing or promising to purchase specified quantities of specific goods and services in a competitive market. If consumers demand more of a certain commodity or service, the price system reflects that increased demand in the form of higher prices, thereby automatically inviting businessmen to increase their supplies. Scores of independent, unrelated decisions by businessmen operating for profit are made as they watch the reactions of consumers as reflected in the market place through the price system. If prices go down, production is presumably curtailed; as prices go up, production is increased. The operation of the price system attracts more public attention in war time than it does in peace time, although its function is no more significant then than at any other time or phase of a business cycle. In war and in peace it is the function of consumers to register their demands in the market place, presumably on the basis of intelligent and rational decisions based upon the knowledge of their own needs and of the goods and services available to satisfy those needs.

The diagram on page 4 attempts to illustrate the nature and operation of our economic system, with emphasis on the central function of consumers. The outer border line—marked Government, Family, Free press, Free speech, Church, and Free public school—designates the framework of political and social institutions within which our economic system functions. The fact that we have a representative, democratic government as one cornerstone of American life, and the

monogamous family as another cornerstone, supplemented by the church, the free public school, a free press, and the freedom of speech, is basically important in understanding the operation of our economy. This is not to imply that all of these institutions have attained perfection, but they are goals which the American people have set for themselves.

Operating within the framework of political and social institutions, is the framework of our economic system indicated by the phrases Free enterprise, Profit motive, Right of private property, Free competition, and Free contract. The profit motive is the keystone in the framework of the American economic system, while the other four economic institutions are cornerstones in the structure. Again it must be said that the "rights" of free enterprise, free competition, free contract, and private property are goals not always fully achieved. One of the functions of government, for example, is to attempt to prevent monopolists from interfering with the rights of others to engage freely in enterprise.

Operating within the framework of economic institutions, consumers are strategically placed as the ones for whom the economy functions and by whom it is controlled, theoretically. As the diagram shows, consumers register their demands in the market place by spending their dollars. In the act of spending, they indicate their preferences for some types of goods and services, and their lack of interest in others. In those cases where preferences are strong, consumer demands would be reflected through the price system in higher relative prices, while lack of consumer demand would be reflected through the price system in lower prices. Under a system of free enterprise, those who have chosen to go into the business of satisfying consumers as a means of earning their livelihood watch the movement of prices, particularly those for the commodities or services which they intend to provide. If prices of those commodities or services start to rise that is an indication that more can be sold, and the enterpriser would be inclined to increase his output. Conversely, if those prices start to fall the enterpriser is notified to restrict his output. Having learned from consumers what is wanted and how much, enterprisers then hire labor, land, and capital for the purpose of producing the desired commodities in the proper amounts. The cycle is completed as processors, wholesalers, and retailers move the goods and services to markets where final consumers can buy them.

Once more it is necessary to recognize that this picture is not nearly so perfect in practice as it is on paper. Indeed, one of the reasons this book is written is to help the reader to examine critically the operation of the economic system from a consumer point of view. In the pages which follow, it will be found that many consumers perform their tasks inadequately; that dollar votes are not as democratic as they appear to

be; that enterprisers attempt to control prices, thereby interfering with the price system; that sellers attempt to influence consumer demand by means of aggressive selling; and that there are also various other frictions and imperfections in the operation of the system. Nevertheless, if we start with a mental picture of the nature of our economic organization it will help us to understand the problems which will be encountered.

Consumer Democracy. Much as we pay tribute to the principles and ideals of democracy, we must face frankly the question, Is our economic life democratic? Perhaps we should ask also, Can our economic life be organized on a democratic basis? Should it be? Democracy has been defined as " . . . that way of life which offers equal opportunity to all individuals to develop to the limits of their capacity."[1] Another concept of democracy holds that it "is a society in which citizens are continuously creating the conditions under which they wish to live."[2]

The concept of economic democracy implies a share in the control of the economic system by the three great groups of people most concerned with its operation—owners, workers, and consumers. This is not the place to discuss the concept of industrial democracy or the problems of concentration of economic control resulting from the corporate form of organization. Our immediate concern is with consumer democracy. This idea implies that consumers shall participate continuously in creating the conditions under which they wish to live. If desirable goods and services are wanted by consumers, it is their privilege and their responsibility in a free-enterprise, free-choice economy to see to it that those types of goods and services are produced. If goods and services are produced which promote consumer illfare, rather than consumer welfare, consumers must accept a large share of the responsibility for that condition. Many of them have abdicated their jobs of intelligent and free-choice making. They have permitted themselves to fall under the charm and sway of habit, custom, fashion, and aggressive selling practices. As a result, their decisions are made for them, rather than by them.

If political democracy is to work, it must be girded up by an understructure of economic democracy. And if economic democracy is to work, consumers must exercise their function of free-choice making intelligently and must assume responsibility for making a free-price system operate effectively. This is not to say that they alone can accomplish all this, but it cannot be accomplished if they do not perform their share of the task.

[1] CHRISTIAN, Johnie, "A Vitalized Program for Home Economics," in *Journal of Home Economics*, September, 1941, p. 447. [2] BROWN, Muriel W., "Education for Family Adjustment Today," in *Journal of Home Economics*, April, 1941, p. 226.

In the pages which follow, the reader will find in this Part One two additional chapters dealing with the question, Who controls the productive process? Then follow, in Part Two, eleven chapters the purpose of which is to encourage and help the reader to engage in a process of critical self-examination to discover to what extent and how effectively he performs his functions and assumes his responsibilities as a consumer. This is done on the theory that unless each one realizes, in part at least, the extent of his deficiency, he is not likely to be very receptive to suggestions for improving or changing his consuming practices. On the other hand, if one finds after an honest self-examination that his freedom of choice is unnecessarily limited because of the influence of custom, fashion, imitation, or aggressive selling, such a consumer is then in a frame of mind to accept suggestions as to how he may perform better the functions which are his, and to assume the responsibility which all consumers must assume if they wish to retain a system of freedom of choice. The remaining fifteen chapters deal with specific aspects of the consumer problem and contain many suggestions for individuals and for groups, all intended to encourage improved consumers' practices.

Can Consumers Function Effectively?

Up to this point the discussion has tacitly assumed that consumers are fully competent to exercise their functions and to assume their responsibilities. It is now necessary to examine this implied assumption critically. In order properly to perform their functions, consumers would have to know first what they want; then, although they would be amenable to suggestions from sellers, they would not be so completely controlled as some are at present. Then it would be necessary for consumers to be able to judge the quality of the things they buy, to know when prices are fair and to what extent competition really operates. If consumers were able to do all these things, they would then meet sellers in the market place on fairly even terms and the results of their bargaining would be reflected in the prices they pay and the quality they receive. There was a time when American consumers possessed these qualifications to a greater extent than they do at present.

A Contrast. In 1776 there were only about 3,000,000 people in the thirteen American colonies, in contrast with the 136,000,000[1] people of the United States in 1943. The transportation facilities were few and very inefficient, so that individuals and groups were compelled to live almost entirely on what they had at hand. Today the United States is bound together not only by over 240,000 miles of railroads and many thousands of miles of paved highways, but also by improved

[1] The exact estimate for January 1, 1943, was 135,604,000.

waterways and many air lines. Measured by transportation facilities, modern Europe is closer to America than the Potomac River was to New York in colonial times. As a result of improved transportation, modern consumers have available all of the resources of this country and of other countries. Their wants have expanded manyfold and their problems of choosing have increased with rapidity. A century and a half ago there were no huge corporations producing commodities on a large scale in anticipation of consumer demand. On the contrary, production was carried on by individuals on a small localized scale after an order had been placed by a customer. Then it could be said with much greater truth that the consumer guided production. Then also it could be asserted with more show of authority that competition was an effective regulator of price and defender of the consumer. If the town cobbler made a poor pair of shoes for a local resident he had to meet the victim of that transaction daily, and the news of a consumer's dissatisfaction perhaps spread throughout the town. Regardless of personal ethics, the cobbler did not dare run the risk of palming off inferior shoes. Much less could the baker or butcher run the risk of selling spoiled or putrid bread and meat. By the very nature of the simple economic life of early times, the consumers, because of their wide variety of interests as producers, were far more able to judge the quality of merchandise offered for sale, and to judge the fairness of prices asked.

In that simple colonial life there were few newspapers and scarcely any magazines to serve as media for bombarding readers with appeals to buy. Mail service was extremely limited, and not yet subsidized for the benefit of magazines and newspapers carrying their millions of words of advertising copy, while direct attack by mail was unknown. There were no radio broadcasting stations with supplementary receiving sets by means of which profit-seeking producers could carry their resonant voices of praise into the very homes of potential buyers. There were no moving pictures to help the producer advertise by visual appeal to the pathetic longing of millions of people for some of the better things in life. There were no airplanes to write their messages in the sky, nor any billboards to mar the scenery and force the attention of the leisurely traveler.

There was no system of compulsory education. There were no schools of business with courses in advertising and salesmanship. There was then no science of psychology to misuse for advertising purposes. Finally, by way of contrast, when a consumer in that system had decided to buy he was compelled in most cases to pay cash or depend upon his own limited personal credit at the local store for a short time, for there were then no banks or finance companies to co-operate with

forceful salesmen by making it possible for consumers to pay a dollar down and a dollar a week.

In the simple economic world in which our forefathers lived it is quite possible that as consumers they knew what they wanted, were able to judge quality, and were aware of any attempt to charge prices far above the costs of producing goods and services. It may have been true also that as producers they were guided by the wishes of consumers and restrained in their seeking after profit by the operation of competition. Yet that assumption is questionable, for the "popular practice of fraud" was even then a well-developed art, though less extensive than it is now.[1] In our modern interdependent, complex economic life these basic assumptions are largely invalid. Myriad forces playing on desires of modern consumers are so varied that the fundamental assumption that consumers know what they want is itself questionable.

Do Consumers Know What They Want? Under the influence of the profit stimulus men as producers have tapped the innermost resources of their ingenuity to create new goods and to render new services which they think they can make consumers want. Whereas the supply of goods offered for sale in a colonial market was comparatively limited, the supply offered in a modern world market is so extensive that it can be asserted safely that millions of consumers do not even know of the existence of many commodities. Certainly this is not because producers have failed to make every possible effort to acquaint potential buyers with the existence of their particular products and to inculcate a desire for them so strong that purchases will result. It is caused rather by a veritable plethora of goods. This is not to imply that all goods offered are good in the sense that they have the power to further human welfare, but suggests that they are offered because producers have found in them a source of profit. Are there any consumers who have not had the experience of window shopping and discovering some new novelty which calls forth the remark, "That is just what I want"? At the moment the consumer is convinced that he or she wants this product which a moment before was unwanted because its existence was unknown. And who has not had the experience of thumbing through the catalogue of a mail-order house and finding descriptions of contrivances wholly new and unfamiliar? In some cases reading the description does not result in a want, while in other cases a responsive chord is struck and a new want is born.

By contrast, is there anybody who has not had the experience of purchasing a commodity, which act in itself is evidence that a want was

[1] Harding, T. Swann, *Popular Practice of Fraud*, Longmans, Green & Co., New York, 1935.

presumed to exist, only to discover after coming into its possession that it is not wanted at all and is discarded and forgotten? A substantial volume of business is based upon the custom of giving presents to others upon such occasions as birthdays, weddings, anniversaries, and Christmas, and as party prizes. How frequently the recipients, especially brides, find themselves in possession of a gift for which they have no earthly use and which they do not want! Evidence of this is to be found in the large volume of exchanges resulting from badly chosen gifts, a form of "busy-ness" which is the main occupation of store clerks during post-holiday periods of dullness.

Many wants are derivative in their origin, and consumers frequently do not know that the purchase of one commodity is going to lead them to want something else necessary to its complete enjoyment. Recently a new-style fountain pen, resembling a mechanical pencil, was offered on the market. It was wanted by some consumers upon their seeing it. After purchasing the pen one discovered that a special and expensive kind of ink was necessary to make it write properly. Upon discovery of that need a new want was created, but certainly the consumer did not know in advance that he wanted that special ink.

There are many other angles to this question of human wants. Do children know what they want? Do adults want what they need? To what extent are their wants original and to what extent acquired? Answers to these and similar questions will be sought in the next chapter.

Can Consumers Judge Quality? An outbreak of food poisoning in Westchester County, New York, affecting several hundred persons, led to a search for the cause. Public health officials discovered that each of the victims had eaten cream puffs from a local bakery. Examination of the bake shop and of workers in it failed to reveal any clue until the search finally settled upon the eggs used. A particularly virulent germ was discovered in some of the eggs. The next step was to discover conditions under which the eggs had been laid and packed. Search led health officers first to several Missouri farms where the eggs were laid, then to a Nebraska wholesale house where they were handled and packed, and finally to a distributing jobber in New York City through whose hands they passed. Somewhere in the process some of the eggs were cracked and infected with germs.[1]

This illustration is but one of many which could be given, showing the complexity and interdependence of our economic life. Consumers in

[1] *New York Times*, April 28, 1935. For similar illustrations of food poisoning resulting from circumstances over which consumers have no control, see *New Hampshire Health News*, June, 1943, vol. XXI, no. 6, for reports on cream pie and canned mushrooms.

New York and in every other locality are daily consuming products produced at great distances by persons they have never seen and never will see. As the volume and variety of goods which modern consumers buy steadily increase, their ability to judge quality becomes progressively less. At the same time the impersonal nature of the economic system renders it easier for unscrupulous producers to dispose of defective merchandise. It becomes but a short step from taking a chance on selling food products of questionable purity to the deliberate process of palming off foods which are known to be decomposed. All that the dealer in such a case sees is the net profit which the transaction yields; he does not see the victims suffering from food poisoning.

That such practices are still common is shown by a perusal of *Notices of Judgment* under the Federal Food, Drug, and Cosmetic Act of 1938 as detected and published by the Food and Drug Administration of the Federal Security Agency. Case 3518 was based on a shipment of canned crab meat from Oak Hill, Florida, to New York City. The cans were labeled "Lagoon Quality Deluxe . . . Crabmeat." The United States attorney charged that the product "was adulterated in that it consisted in whole or in part of a filthy animal substance." No one appeared to answer the charge, so the product was ordered destroyed.[1]

Many American people literally live out of tin cans, the quality of whose contents they have no practical way of judging. To be sure, death or illness may prove the nature of the contents, but that is of small consolation to the victim. Moreover, there are many kinds of ailments attributed to food poisoning which are not easily or readily detected. One may assimilate portions of lead in one's food for a long time before any ill effects are noticed, and then it is too late.

When we turn from food products to other types of commodities, the task of detecting quality is found to be no easier. Are the life preservers on a modern ship carrying thousands of passengers made of genuine cork? Are the tires on which millions of automobilists trust their lives made of genuine virgin rubber? Are the steering gears on automobiles so designed that they will not lock? Is the electric insulation in the house which one rents or buys of first quality and properly installed so as to prevent fire hazard? Are drug prescriptions properly compounded and do they consist of pure drugs? Are the mattresses on which one sleeps made of new and first-quality materials? Are the blankets and clothing upon which one depends for warmth and comfort really made of wool?

Many pages could be filled with similar questions, but in all cases

[1] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act,* March, 1943, Number 3518.

the answers would be the same. Not only do consumers not know how to judge quality, but they cannot know. In the absence of laws to protect them their very lives are in the hands of producers. So completely has the economic system changed that the assumption that consumers are able to judge quality is almost entirely without foundation.

Can Consumers Detect Price Frauds? The very bewilderment and helplessness of consumers lead many of them to depend upon price as a measure of quality. Knowing their inability to test the quality of a commodity, they assume that low price is evidence of inferiority and that high price is a guarantee of quality. But again the producer has the advantage and makes the most of it. He knows that very few consumers have any idea of the costs involved in making his commodity. Under these circumstances it is possible for some producers to market inferior products at high prices. They are enabled to continue by the very fact that consumers have no way of comparing the quality of one product with that of a competing product. In two different stores located in Bismarck, North Dakota, enforcement officers of the State Laboratories Department purchased identical-sized cans of beets. Laboratory tests revealed a cost of nine cents per pound for one can which graded A, while another can which graded C cost fifteen cents per pound.[1] Additional illustrative evidence will be found in Chapter 13.

The concept of fair price is relative rather than absolute. In order to arrive at an intelligent conclusion concerning the price of a commodity, one must know what it costs to produce a product of that particular quality. So far as the consumer is concerned, a can of beets is a can of beets, and a can of crab meat is simply a can of crab meat. Yet between two cans of similar appearance there may be a vast difference in quality with no difference in price, or there may be wide variance in price and no difference in quality.

What, if anything, does the consumer know concerning the cost of producing a can of beets or of crab meat? For generations economists have pursued the elusive answer to the question, What determines price? Reference to a standard text in elementary economics will show that as much as twenty or twenty-five per cent of the book is devoted to an attempt to explain the factors determining price. If one wants evidence of the difficult intricacies involved in determining costs of production, let him turn to some of the cost studies made by the United States Tariff Commission. When the problem becomes so complicated that economists, cost accountants, and executives cannot determine the exact cost of producing some commodities, it is nothing short of naïve

[1] State Laboratories Department, *Bulletin No. 67*, Bismarck, North Dakota, June, 1942, pp. 77–79. Many similar price disparities will be found in this Bulletin.

to expect the average consumer to have any intelligent opinion concerning the fairness of the prices of any significant variety of goods.

In the realm of necessities there is without doubt sold over the counter daily a large volume of merchandise at prices which bear a close relation to its costs of production. But when we turn to the enticing fields of patent medicines, insecticides, cosmetics, soaps, paints, varnishes, refrigerators, bicycles, cleaning fluids, metal and furniture polishes, flatirons, eye-glass frames and lenses, and scores of other commodities which consumers buy daily, less relationship is found between costs of production and prices. If the reader desires evidence of consumers' inability to judge price let him turn to Chapter 13 or to The Twentieth Century Fund's answer to the question "Does Distribution Cost Too Much?"[1]

Does Competition Regulate Prices? The assumption that rivalry in buying and selling will operate to the consumer's advantage by holding prices down to, or near, costs of production must be seriously modified in modern economy. The present economic system is one in which competition is an all-pervasive force. Properly and completely understood, the description of capitalism as a competitive society is correct, but while competition may prevail in large areas and on a broad scale there may be at the same time important smaller areas in which competition is restricted or absent.

Development of modern business under the corporate form of organization, with its offspring the holding company, has been characterized by constant and apparently increasingly successful efforts to secure complete or partial monopoly control. Buttressed by trade associations, open price agreements, and resale price-maintenance laws, American businessmen have still further shattered any faith the consumer may have left in the efficacy of competition.

Even though the force of competition may operate, it is of little or no benefit to the consumer if it leaves prices far above the cost-of-production level. In many such cases one might contend that competition prevails, but if so, and if by common agreement the retail selling prices are kept far above costs of production, the competition is of no benefit to the consumer.

Historically, the idea prevailed that all competition is desirable. While that may have been the case in colonial times it certainly is not true today. Students of economics are familiar with that type of business which economists describe as a natural monopoly of organization. In the cases of modern railroads, telegraph lines, and electric light

[1] STEWART, Paul W., and DEWHURST, J. Frederic, *Does Distribution Cost Too Much?*, The Twentieth Century Fund, New York, 1939.

and power, gas, and water supplies, the operation of competition may cost the consumer more in the long run and result in a higher rather than a lower price. In the twentieth century this has been extensively recognized, so that today many of these businesses are granted monopoly privileges under condition that their prices are subject to control by official Commissions representing consumers. Another field in which competition is wasteful rather than beneficial is found in the exploitation of natural resources such as coal, oil, and timber. Natural geological conditions which govern the supply of these and similar commodities are such that the maximum product can be gotten at a minimum cost under conditions of monopoly or co-operation rather than competition.

Is Market Price a Measure of Subjective Value? For purposes of economic analysis it is assumed that when consumers enter the market and pay the prevailing prices for commodities offered for sale these prices are a fairly accurate indication or measure of the subjective values placed on the commodities by consumers. If all consumers had equal purchasing power, if all were equally well trained as buyers, and if all goods were honestly made and priced, then, and only then, would prices really reflect the subjective values.

In reality consumer purchasing power varies so greatly, the ability of most consumers as buyers is so limited by their lack of knowledge of the complicated system in which they live, and finally there is so much adulteration and falsification on the part of producers, that it is simply impossible to assume that if each of two buyers pays 11 cents for a loaf of bread their subjective valuations are identical.

If all persons had equal purchasing power the willingness of two consumers to pay 11 cents would more nearly reflect their subjective valuation of the bread. But the law of diminishing utility applies to money as to all commodities, and one who enjoys an income of several millions of dollars a year will value each additional dollar much more lightly than will the person whose income is limited to a few hundreds or thousands of dollars a year. The latter consumer will value his 11 cents much more highly than the former, and his exchange of those pennies for bread would be an indication that the use value of bread is very high. The fact that national income is so unevenly shared by consumers leads to considerable waste in economic life in that the wealthy few with their many dollars have a disproportionate power in determining the types of goods and services produced. Since the principle of diminishing utility does operate we find wealthy consumers ordering producers to build palatial homes, luxurious yachts, and racing stables before large numbers of consumers have had even the bare necessities of a decent living standard.

A greater equality in purchasing power would not be sufficient to overcome the objections to the assumption that price is an accurate measure of subjective values. To the casual observer it is apparent that some consumers as buyers are much more shrewd than others, knowing better how to judge quality and price and being more adept at bargaining or haggling, a practice from which most consumers shrink. All of this is to say that some consumers more nearly approach the concept of the economic man, but their number is small. If all consumers had such knowledge and bargaining ability in addition to equal purchasing power, the prices paid by them would much more nearly reflect each individual judgment of use value.

Under a system of production as highly specialized as ours has become, it is a natural consequence that in most cases producers are much more shrewd and much better informed about their particular goods than consumers. Under these conditions it follows that producers can sometimes adulterate their products with impunity, since no one but a trained chemist would be able to detect the presence of the foreign substance used.

Who Does Guide the Economic System?

For purposes of economic analysis it has been assumed that all persons as consumers and as producers act as economic men. Consumers are presumed to know what they want and to be able to judge quality and price. Their willingness to pay the market price for a commodity is an assumed measure of the subjective valuation placed upon that commodity and also is an indication to producers as to what they should produce, how much, and of what quality. In this spontaneous co-operation competition is the policeman that regulates price and protects consumers from producers and producers from one another. Although they do not know it, consumers are described as the leading characters in this economic drama—characters whose slightest whim reflected in the market place is the signal which sets producers busily to work to satisfy their wish.

Examination of the validity of the several assumptions upon which this explanation is based reveals that some of them must be modified, in the light of a changed economic world, to the point almost of elimination, while all of them must be modified in part. If this explanation of the guiding force in the economic system is not accepted, who may we say does guide and control this system?

The discussion in this chapter suggests that consumers alone do not guide production. It shows also that their part in guidance is very poorly performed. It appears that the producers share with consumers the

task and the privilege of determining what shall be produced. But in order fully to answer the question as to who guides economic life we must examine the nature and origin of human wants, as is done in the following chapter. If we can discover the sources of wants and the forces playing upon them we shall then be able to answer the question.

Summary

It has been assumed that consumers are "economic men" who unconsciously guide and control the economic system. They are presumed to determine, through the price system, what shall be produced, how much, and of what quality. Critical examination of the five assumptions on which this explanation depends reveals that while they may have been justified one hundred fifty years ago they are not now tenable. Consumers do not always know what they want; their inability to judge quality and to detect price frauds increases. Market price is not a measure of subjective value, nor does competition adequately regulate prices in consumer interest. This being so, it can scarcely be maintained that consumers alone guide the economic system. The producers' share in that guidance and control will be considered in later chapters—especially 3, 10, and 11.

QUESTIONS FOR DISCUSSION

1. Were you aware previously that as a consumer you have an important function to perform in the economic system?
2. What is the economic function of consumers? How is it supposed to be performed?
3. Compare your abilities as a wise consumer with those of your great-great-grandparents; list the significant changes which have taken place.
4. Do you always know what you want?
5. Have you ever purchased a commodity, thinking you wanted it, only to learn that you really did not want it?
6. What is a derivative want? Give several examples.
7. Illustrate what is meant by "the impersonal nature of the economic system." How does this development affect you?
8. Describe the worst rooking you have ever had—the most expensive cheating in a purchase you made.
9. On the last purchase you made did market price measure accurately your subjective valuation? How much more would you have been willing to pay?
10. Do you think competition is effective in your local market? What do you mean by "effective"?
11. What *is* a fair price for a commodity?

PROBLEMS AND PROJECTS

1. Test your ability to judge quality by comparing five different brands of bread. Do the same for ice cream, milk, coffee, and any other articles you particularly wish to include.

2. Vary the procedure above by bringing your five samples to class. Let each member of the class rate the brands according to his ability to judge quality. Compare your final results. Then ask some qualified member of a chemistry class to test comparative qualities in the laboratory.

3. Do you think competition assures identical prices for goods of the same quality? Select five or ten nationally advertised products such as Camay soap, Carnation milk, or Whitman's chocolates and compare their prices in five different stores located in the same market area.

4. Compare your subjective valuations for a selected group of commodities with those of other members of the class. List the price you would pay for each article rather than go without it; then compare results with the prices quoted in the market. Is market price a measure of subjective value?

5. If you have relatives or friends in some manufacturing business ask them to give you the actual cost of manufacturing their product; add to that the cost of marketing; then compare that figure with the retail selling price. How capable are you of judging the fairness of retail prices?

2

Consumers' Choice

The Consumer and His Wants

Unlimited Wants Versus Limited Resources. Economic theory takes as its starting point two supposedly basic facts of economic life. The first of these is the insatiability of human wants. It is presumed that as human beings our desires for goods and services are capable of indefinite expansion. Most writers on economics accept this as a basic fact so obvious that it requires no demonstration. A few attempt to establish the fact by use of the historical or comparative method. The limited wants of our ancestors are compared with the much wider range of wants of present-day consumers. Consumers today want and expect to have an abundance of food, including many products unknown to their ancestors, and a comfortable abode heated with coal, gas, or oil, well-decorated and finished with attractive walls and floors, and comfortably furnished and equipped with such modern furniture and appliances as overstuffed living-room sets, seven-tube radios, walnut dining-room furniture, bird's-eye-maple bedroom suites, porcelain bathroom equipment, hot and cold running water, gas stoves, electric toasters, ironers, and refrigerators, and numerous other articles deemed necessary to maintain a modern plane of comfortable living. It is commonly asserted that the modern middle-class family lives more luxuriously than royalty of old. Yet modern middle-class families are not satisfied, and economists contend they never will reach the stage of complete satisfaction.

In using the comparative method of demonstrating insatiability of human wants, planes of living of contemporary groups may be compared. Although a middle-class American family lives in luxury as compared with persons living in economic systems which have not developed the same high degree of efficiency in turning out material goods, they are none the less dissatisfied in the sense that they still want more. If middle-class American families living in their comparative luxury complain of unsatisfied wants, how much more, it is argued, are the wants of those less fortunate ones in lower-income groups capable of indefinite expansion? Not until every consumer in the nation has satisfied every possible want can we properly speak of a point of saturation, and by the time that point is reached new goods will have been developed which

consumers will want, and so the process will go on indefinitely. In fact certain students of business cycles contend that each new period of prosperity is initiated by the development of an industry producing some comparatively new commodity or service which large numbers of consumers do not yet have but desire. Thus it was automobiles at one time, radios at another, and predictions vary as to whether the next major development will be in the field of electrical appliances, air conditioning, or air transportation.

Among economists practically no attempts have been made to test the theory of insatiability of human wants by inquiring into their psychological origin. When economists and psychologists collaborate in such a venture our knowledge of human wants will be vastly enlarged.

The second of the basic economic facts is described as the niggardliness of nature. This is based upon the demonstrable fact that in any given stage of economic development the application of continually increasing amounts of labor and capital to a fixed amount of land will yield progressively smaller returns after a certain point has been reached which economists call the point of diminishing returns. This is in fact a physical law capable of demonstration, and its economic consequences are far-reaching. The modern version of this principle, known as the law of variable proportions, renders it still more comprehensive, since the principle of diminishing returns will operate in any possible combination of the factors of production. In the past centuries consumers have largely escaped the consequences of this law as a result of numerous discoveries of new land. So far as we know, the entire world has now been explored, so that this avenue of escape appears to be closed. But another force helping to offset the tendency toward diminishing returns has been the application of human ingenuity to new and more effective ways of utilizing the scarce resources available. There are those who adhere to the philosophy that necessity is the mother of invention, and contend that mankind will always find new methods of producing wealth when the pressure becomes sufficiently great. While this is a comforting view it is scarcely a satisfactory one. In spite of the parrotlike repetition in popular magazines of the euphonious phrase that we have poverty in the midst of plenty, the implication of the latter part of the statement is not borne out by a survey of our potential productive capacity.[1] According to these studies we do not have an abundance of economic goods and services, and there is no sound reason for believing that we shall ever overcome the problem of scarcity sufficiently to provide a Utopian plenty.

[1] NOURSE, E. G., and Associates, *America's Capacity to Produce*, The Brookings Institution, Washington, 1934. LOEB, Harold, and Associates, *The Chart of Plenty*, The Viking Press, New York, 1935.

Unlimited wants of consumers, in the face of limited resources with which to satisfy those wants, create the central and eternal problem of scarcity with which economics deals. Since man as a producer cannot produce enough to satisfy his wants as a consumer, the problem arises, Whose wants shall be satisfied? In a capitalist economy scarce products are valued according to their costs of production, and the power of individual consumers to acquire them is determined by the importance of their contribution of labor, land, or capital as measured by their marginal productivity. The central struggle of economic life thus becomes a contest to determine which of the unlimited wants of consumers will be satisfied.

What Constitutes Happiness? If happiness is defined as a state of pleasurable content with one's condition of life it is pertinent to inquire whether such a state is to be achieved by struggling to acquire enough wealth to satisfy more of our unlimited wants, or whether the road to happiness is to be found by limiting wants within the extent capable of satisfaction by our limited resources. The first method leads to a materialistic philosophy of life which, carried to its logical extreme, becomes sheer sensuous gluttony. To followers of such a philosophy the only satisfactions and hence the only happiness they know is achieved through the utilization of those material goods which temporarily satisfy various physical senses. Since a characteristic of appetites of all kinds is that they feed upon themselves, happiness of this sort can be achieved and maintained only by an increasing amount of goods. There is no place in materialist philosophy for any immaterial values, any consideration for the welfare of others, or any concern for the baffling question of immortality. It is eat, drink, and be merry, for tomorrow we may die.

So-called Western civilization in the nineteenth and twentieth centuries has frequently been described as motivated by this philosophy of materialism. With its increasing ability to make more machines to make more goods, it is alleged that those living in this civilization are swept into the belief that the only way to achieve happiness is to get more and more goods.

The second method of achieving happiness leads to an ascetic philosophy of life in which the practice of physical self-denial is elevated to a virtue. A crust of bread, a cup of goat's milk, and a glass of water are sufficient to meet the physical needs of the exponents of this philosophy. Time which materialists waste in seeking after the temporal things they want is spent by ascetics in leisurely thought and meditation, with emphasis upon the mysteries of life and death and the world beyond. This philosophy is usually, though not necessarily, associated with some form of religion. By all standards of comparison the physical scale of

living throughout the Orient is lower than in the Occident. Yet it is contended that the millions of inhabitants of the Far East are not only not unhappy but are positively happy; and that it is only when Western missionaries or other emissaries from the Western world inculcate in them a psychological desire for things never before wanted that dissatisfaction verging upon unhappiness results.

One of the telling criticisms against religion of whatever kind has been its universal tendency to exalt the ascetic over the materialist philosophy. Marxian Socialists in the middle of the nineteenth century charged that religion and the church had become opiates to the masses. It was claimed that although royalty and those other few favorites at court were free to enjoy all the good things of this life their supply was so limited that the masses were completely deprived of them, yet failed to rebel against such a system because their religion promised them that they would inherit the earth in the life hereafter.

To an impartial observer there does not appear to be any fundamental quarrel between these two philosophies. Both have their values, but either one carried to an extreme results in a distorted view of life. A balanced plan combining the virtues of both philosophies seems to yield real happiness. While it is true that man does not live by bread alone, it is also true that he cannot live completely on meditation. If material wealth is properly regarded as a means toward an end it becomes a necessary adjunct to that richer and more abundant life which the Nazarene came to bring to all people.

Nature and Origin of Human Wants

Distinction between Wants and Needs. It has been estimated that about one hundred years ago consumers had 72 wants, of which 16 were necessities, in contrast with modern consumers who have 484 wants, of which 94 are necessities. In a narrow economic sense necessities or needs are limited to those forms of wealth which are indispensable to the maintenance of life. These would include a minimum of food, clothing, and shelter at least sufficient to maintain the physical strength necessary to provide these very necessities. A popular American fallacy is the belief that all consumers in this country are supplied with these fundamental needs and that most of them are able to satisfy additional, less essential desires. In his inaugural address as president of the American Medical Association, Dr. James S. McLester stated that "something like twenty million American people are living near or below the threshold of nutritive safety. This condition, if continued, will surely affect the health of the race."[1] An even more serious picture is presented in

[1] *New York Times*, June 12, 1935.

the findings of family food consumption made by the Bureau of Home Economics of the United States Department of Agriculture. The report shows that not more than 25 per cent of the families in the United States had diets that could be rated good; the diets of more than a third could be considered only fair; the diets of another third or more were definitely classed as poor.[1]

Economic want may be described as the state of being without something which is desired. Consumers want many things which are not essential to life itself but which are necessary for a more complete, abundant life. Many consumers want things which actually retard rather than promote their economic welfare. How are these wants in contrast with needs to be explained? What is their origin? Why do consumers want what they want?

Human Wants Classified. With reference to their origin, human wants may be divided into two major groups: (1) those individual, inborn tendencies characteristic of all humans, and (2) social or group wants.

By some writers the individual, inborn tendencies of the first major group are called instincts, and the literature of psychology is filled with controversy over the question as to what human traits are instinctive. Whether these traits be called inborn tendencies or instincts, their essential characteristic is the involuntary motivation to action which results in expression of a want. The inborn tendency explains the want, while the mind, valuing objects and situations externally, chooses for its satisfaction. For our purposes it is not necessary to decide or even to discuss the question whether these actions are instinctive or not. The question is important, but one to be handled more competently by psychologists. For us the real question is whether these inborn tendencies are so universal and unmistakable as to be constantly reckoned with in analyzing and explaining the economic conduct of consumers.[2]

In seeking to avoid the implications and connotations attached to the words "needs," "wants," and "desires," Professor Hoyt turns to the word "interest," defining it as an economic choice concretely ex-

[1] STIEBELING, Hazel K., *Are We Well Fed?*, Miscellaneous Publication No. 430, United States Department of Agriculture, Washington, D. C., 1941.

[2] KYRK, Hazel, *A Theory of Consumption*, chap. 9, Houghton Mifflin Company, Boston, 1923. KITSON, Harry D., *The Mind of the Buyer: A Psychology of Selling*, chap. 11 (The Macmillan Company, New York, 1921) refuses to list all instinctive acts but recognizes at least seven and classifies these according to those which preserve life and welfare of the individual, those which provide for continuance of family and race, and those which promote welfare of the tribe or social unit. PARKER, Carleton H., "Motives in Economic Life" in *American Economic Review*, December, 1917, vol. 8, p. 212, recognized and listed sixteen instincts which he regarded as unlearned and universal.

pressed. In her judgment the first interest establishes itself through the physical mechanism of the nervous system. In the case of primitive man the first difficult step was that of bridging the gap between realization of an interest and its satisfaction. For consumers in a civilized society this bridging process is simplified, but at the same time influenced, by established customs of the group. For many consumers new interests are established only with difficulty, usually through the process of association or imitation. Habits, defined as a settled disposition or tendency to action due to repetition, are quickly formed.[1]

First and probably most basic of these inborn tendencies, instincts, or interests is the universal human desire for food and drink. While a starving man will eat and drink almost anything, this condition of stark privation is not common among groups which have attained an organized system for producing the goods with which to satisfy their wants. For most consumers individual preferences based upon physiological differences quickly reveal themselves. One child will like cod-liver oil, while another will take it only under compulsion; one will eat spinach and like it, while another will not eat it at all; one will insist upon chocolate-flavored ice cream, while another will eat only that flavored with vanilla. These physiological differences in taste seem to be inborn. But Dr. Clarence Mills thinks that taste depends upon one's sense of smell. Limited evidence indicates that people temporarily deprived of their sense of smell complained that food had lost its taste.[2]

For most consumers the desire for a large part of their food and drink is acquired rather than inborn. By persisting one can acquire a taste for many things which are at first instinctively shunned. Most consumers fall within that group whose choices of food and drink are determined as much by the palate as by that inborn tendency called hunger. Taste for such nonessentials as tea, coffee, and intoxicating liquors is invariably acquired.

A second basic individual want is that for some type of shelter to afford protection from the elements. Ranging from the cave abode of primitive man to palatial homes of modern men of wealth, this desire for protection from wind and rain, heat and cold, reveals itself in an extensive consumer demand for a wide variety of goods. A large segment of human wants can thus be explained, from demand for lumber, brick, stone, steel, and concrete, to more delicate objects of decorative art. Although it is estimated that some eleven million people are living in

[1] Hoyt, Elizabeth, *The Consumption of Wealth*, chaps. 1, 2, 3, The Macmillan Company, New York, 1928. [2] Mills, Clarence A., *Climate Makes the Man*, p. 111, Harper & Brothers, New York, 1942.

substandard dwellings in this country, it is still obvious that for most consumers the desire for shelter has been expanded as the result of a large number of acquired wants.

A third basic human want is that for clothing. An attempt to trace the origin and development of modern clothing standards will be made in a later chapter. Considerable controversy has developed over the question whether desire for clothing was first motivated by the wish for protection or whether it was adopted primarily for its decorative features. Whether desire for clothing is inborn or acquired and whether its purpose is to yield protection or to provide ornamentation, it is certain that a large part of consumer income is expended to satisfy this fundamental want.

Humans have a deep-rooted desire not only to live but to enjoy good health. Fortunately there are few people who "enjoy" poor health. The whole medical profession and other curative practitioners with supplementary hospitals, sanatoria, and convalescent homes, together with all their equipment, have sprung into existence in response to this fundamental human want. Nor is this all. Certain profit-seeking producers have found this a lucrative field in which to apply their practices of quackery in all its numerous variations.

For our purposes the next two basic human wants may be considered together. These include love for the opposite sex and love of children. The former is likely to result in consumer demand for objects of display and for a wide range of commodities to be used as gifts and tokens. Whereas the primitive hunter brought back to the object of his affections gifts indicative of his prowess in the chase, the modern hunter goes forth to acquire money with which to buy lavish gifts as evidence of his acquisitive ability. Love for children brings out some of the finest traits in human character. Parents will deprive themselves unhesitatingly of things they may want or even need, so that their children may have proper food, clothing, shelter, toys, and education. Indeed it may be said that an entire modern industry is based upon the single childish desire for toys.

Man appears to be born with a gregarious tendency. This is reflected in the universal human desire for companionship and friendship. It is difficult to determine exactly in what ways and to what extent these basic desires result in concrete economic choices, but that they do so result there can be no doubt. For some people the desire to secure admission to a group for the sake of companionship may lead to copying the economic choices of the group, while in the case of others the desire to attract attention will result in conspicuous and lavish display. Probably the greater part of social life in the narrower sense is motivated by

these two basic desires and is reflected in that wide range of consumer demand for "party" food, decorations, and gifts.

Somewhat different in their nature are the innate tendencies toward curiosity, manipulation, and constructiveness. Man is essentially a curious creature, as a result of which he may be induced to try almost anything new at least once. A wide variety of constantly changing goods described as novelties are produced in response to this tendency. The business of writing and publishing newspapers, magazines, and books is based in large degree upon the curiosity of readers. It may also be said that to a large extent the system of formal education which is so highly developed in the United States finds its basis in this characteristic. Modern merchandising methods provide for the open display of goods so arranged that prospective buyers may satisfy their wish to handle and to manipulate. The constructive instinct is responsible for a large number of concrete economic choices ranging from sand piles and molding clay for children to carpenter's tools and sewing materials for adults.

American culture offers numerous outlets for human tendencies toward play, sport, and adventure. It is a long step from the simple games of primitive man which made use of materials at hand, to the modern scene which supports an enormous industry devoted to supplying sports goods ranging all the way from modern (knightly) football armor to the Pogo stick. Modern fishermen and hunters require for their satisfaction an elaborate and imposing array of equipment. Water sports are no longer confined to those fortunate ones who live on the shores of natural bodies of water, for the ingenuity of producers has brought swimming pools into many an inland village.

The second major group of human wants may be described as those social or group wants which include language, religion, government, art and beauty, and stimulants and sedatives. Perhaps these are not all the wants which should be included in this classification, nor is it at all certain that those mentioned are exclusively social as distinguished from individual wants. But these five fundamental group desires are illustrative of this type of want in contrast with the more narrowly defined individual want.

If there is any one characteristic which sets man off from all other animals it is his ability to communicate his thoughts to contemporaries and posterity through the medium of speech and writing. Every human group has its language. From the hieroglyphics of Egyptians to the equally but quite differently artistic work of modern printers the universal desire of groups to communicate has resulted in derivative wants for pens, pencils, paper, ink, erasers, linotypes, printing presses, and so on through a wide range of supplementary materials.

The recognition of some form of superhuman or overruling power, which we call religion, seems to be characteristic of all peoples at all times. This recognition is evidenced in various forms of worship, which vary from the sun dance of certain North American Indian tribes to the elaborate ritual of the Roman Catholic Church. So deep-seated is the religious feeling in human beings that millions of them willingly forgo material money-bought pleasures for the immaterial values which their religion yields. Money spent for religion results in satisfaction of the human wants for outward expression of religious feeling. A significant portion of our economic life is devoted to the creation of goods and services designed to satisfy these wants.

Wherever people live in groups, whether large or small, we find some form of central authoritative control which we call government. To a nation of 136,000,000 persons the process of government assumes an increasingly large proportion of the economic activities of its inhabitants. While this form of group want is largely satisfied by direct personal services, the very process of governing requires building materials and equipment of an increasingly wide variety. There is a significant tendency for consumers to use their governmental system either to regulate more rigidly the economic activities of producers within the group or, failing that, to have it perform some of those economic services itself.

Recognition of and appreciation for beauty in the world in which we live is a universal group characteristic. This finds expression in various forms of art, which, like language, is a medium of expression to posterity as well as to contemporaries. The more common forms of art expression are drawing, painting, sculpturing, and architecture. From the crudely carved or painted stone of prehistoric man to magnificent modern galleries of art this form of group want has absorbed a significant portion of economic activity.

A curious form of group want is that for stimulants and sedatives. Every people has its intoxicating drinks designed to stimulate, and its narcotics whose purpose is to produce a condition of stupor or coma. While explanation of this phenomenon is too involved to undertake, it should be noted that the objective leading to the use of these products is to a large extent the desire of the users to lift themselves temporarily out of the drab world in which they live. In response to this desire a significant group of producers has developed an important industry whose contribution to human welfare may well be questioned, but whose economic importance cannot be doubted.[1]

[1] For a discussion of human wants refer also to Nystrom, Paul H., *Economics of Consumption*, chap. 4, The Ronald Press Company, New York, 1929; and Chase, Stuart, *The Tragedy of Waste*, chap. 4, The Macmillan Company, New York, 1925.

Economic Resources. The economic resources available to various groups limit the range of their wants, as does the climate in which they live. The influence of climate and resources not only upon group wants for economic goods but also upon ideas is well illustrated in Professor Smith's contrast between the concept of hell held by those who live in tropical and semitropical climates compared with that of inhabitants of a frigid zone. To most of us "hell is hot," but to the Eskimo hell is cold.[1] In the realm of economic wants, residents in tropical climes do not want coal, nor wool, nor furs, while they do want artificial cooling devices and light-weight clothing.

It is apparent that the inborn tendencies in the individual attempt to realize themselves in accordance with environment. All individuals, no matter where they are born, want food, but the kind of food they want is determined by what is available. American children want prepared cereals, Chinese children want rice, while Eskimo children want blubber.

All human beings want shelter from the forces of nature, but the kind of shelter they want varies according to the environment in which they live and to the materials available. The children of many North American Indians wanted tepees, while the children of white pioneers in the same regions wanted log houses in timber lands, sod houses on prairies, and stone houses in stony areas. Some Eskimo children, instead, want and expect to have igloos made of snow blocks.

The amount and type of clothing which people want is also conditioned by their environment and by the materials at hand for use. Many living in the tropics want no clothing at all or at most a loin cloth. By contrast, those living in the frigid zone want furs, both because they are warm and because they are available. In the damp and chilly climate of England warm woolens are desired, but in the sunny southland of the United States cotton clothing is commonly wanted.

Beyond these life-sustaining essentials other wants for luxuries, ornaments, styles of architecture, religious ceremonies, and games are also influenced by climate and by the materials available. The decorative headdress of an Indian chief is composed of feathers, while the jewelry of an Eskimo consists of bones, teeth, and tusks of fish, seal, and walrus.

As economic life advances and transportation facilities are developed, consumers are less restricted to local resources in satisfying their wants. In fact a curious inversion takes place which leads consumers to prize highly for purposes of display products which have come from distant

[1] SMITH, J. Russell, *Industrial and Commercial Geography*, Henry Holt and Company, New York, 1913; new ed., 1925.

places. The way in which tariffs and taxes interfere with or supplement this tendency will be discussed in the latter part of this chapter.

Occupational Activity. What Hobson calls the industrial factor limits and conditions the consumers' range of wants. In their capacity as producers people engage in occupations most of which require special supplementary equipment. Agricultural workers want abundant, substantial food and durable clothing. While engaged in their occupational activities they do not want delicate foods which appeal only to taste, nor do they want fragile clothing for decorative purposes. Rather, their demand is for straw hats to protect them from the sun, heavy shoes in which to follow the plow, and overalls of durable denim to protect their bodies.

Similarly, coal miners want warm, heavy clothing, waterproof shoes and a special kind of cap with lamp attached. Workers in flour mills and bakeshops want light, white clothing, while chauffeurs and pilots want trousers reinforced at the seat, knees, and elbows, and goggles to protect their eyes. Policemen want thick, solid shoes, while sailors want rubber boots and oilskins. Office workers want light food, comfortable chairs, desks, pens, pencils, and ink. As these random illustrations show, an important group of consumer wants is determined by the nature of the work in which the consumers are engaged.[1]

Group Ideas. The influence of the group into which one is born is reflected in a number of ways. For members of a particular group certain wants are customary, while others are taboo, according to the group concept of their survival value. Thus in every group there are certain articles or combinations of food which are shunned by all members in the belief that their consumption would produce illness or death. The tomato, which strikingly resembles the deadly nightshade, has been included in approved diets of some groups only a comparatively short time. There are still many people who do not use mushrooms, because of their similarity to poisonous toadstools.

A curious and unfortunate aversion to cheese has developed in the United States in the belief that it is extremely difficult to digest. The origin of this idea is probably to be found in the American custom of serving cheese with pie as dessert after a heavy meal. When indigestion followed overeating, it was attributed to the cheese. Laboratory experiments have established beyond question the fact that cheese, instead of being difficult to digest, is one of the most easily digestible and nutritive foods.

Some people are prejudiced against eating both lobster and ice cream

[1] Hobson, J. A., *Work and Wealth*, chap. 10, The Macmillan Company, New York, 1914.

at the same meal, or likewise against milk and fish. Perhaps at some time in the distant past some large number of people suffered an attack of food poisoning, and popular opinion attributed it to one of these combinations. Such opinions are handed down from one generation to another and thus become group taboos to all except those adventuresome few, found in any group, who are willing to risk illness and group disapproval by eating the combination to demonstrate the falsity of the group belief.

Similar illustrations might be given showing the influence of the group concept of survival value as reflected in the type of clothing, style of architecture and construction of buildings, and in still other ways. In the Near East, for example, it is customary for all children and most adults to wear a warm woolen band around the middle of the body so as to cover the stomach, in the belief that this affords protection against the dreaded malaria. In jungles houses are built on stilts, and in earthquake areas they are made of light, flexible materials. In both cases the influence of the group concept of survival value is apparent. This discussion borders so closely upon the influence of superstition and custom that further consideration of it will be deferred until those subjects are reached.

The second major manner in which the influence of the group is evidenced is to be found in the case of certain wants which are encouraged or discouraged on the basis of the group concept of their prestige value. If necessary some individuals will develop a nasal twang or a southern drawl in their speech to win admission to a group in which one of these achievements is an indication of prestige. If an individual cannot by some means secure the privilege of wearing a military uniform he may join some one of the numerous secret societies which set themselves off by wearing far more elaborate costumes than any ordinary army could afford. If a young man in London wants to be a bank clerk he must supply himself with morning coat and top hat, and to qualify for admission into this group he must also supply himself with approved evening wear for social occasions. In our own land of compulsory education so many of the children graduate from high school that there is no unusual distinction to be gained by wearing academic costumes at graduation. But only a small proportion of high school graduates are able to continue through college or a university. The college graduates therefore parade their prestige by setting themselves off from others with degrees and academic garb.

These illustrations will suggest to alert readers other similar evidences of consumer choice determined by a group concept of prestige. It is simple enough to understand why individuals bow to a group edict. The gregarious tendency in most people is so strong that they will do almost anything and ask no questions in order to win admission to a group.

But how shall we explain group acceptance of these ideas? Why does one group wish to set itself off from another? Just as one individual seeks to command the attention or respect of others by his exploits, so a group of individuals seeks to command the admiration, respect, or envy of other groups. The origin of this desire to excel is to be found perhaps in the joint operation of a number of inborn tendencies. Love for the opposite sex will lead a man to do strange and unusual things to win the admiration of his beloved and the jealousy of his rival. In former times these exploits were largely limited to the hunt and battle, but in modern economic life the measure of success is often the size of one's monetary accumulation. Wealth thus becomes a symbol possessing high prestige value. Conspicuous use of such wealth is so important a part of the explanation of human wants that a more detailed discussion of it is reserved for Chapter 7.

While we do not recognize the existence of a caste system in American life, one exists none the less. Society is stratified into a number of levels. The pecuniary level is only one of several. The college-graduate caste has already been mentioned. The military caste regards itself as sufficiently superior to set itself off from other groups by adorning itself in a special costume. So also does the clerical caste. In the opinion of most members of these various groups their own group is superior to all others. From an economic point of view this desire for distinction is important in helping to explain the wants of consumers for particular types of goods as necessary badges of membership. This is what Hobson calls the conventional factor in determining human wants. The element of organic utility has largely been supplanted by the influence of conventional utility. Since standards for measuring conventional utility are even more uncertain and elusive than those for measuring organic utility, the opportunity for extensive waste is created.

A third way in which the influence of one's group is reflected is to be seen in the case of certain wants which are frowned on or favored on the basis of the group concept of welfare.[1] This is a much broader concept than either of the other two and consequently more difficult to detect and isolate. There is, in fact, some repetition, for the group concept of what constitutes and promotes its own welfare may include education, religion, military prowess, artistic achievement, economic security, to mention only a few. It is apparent that the German concept of group welfare as reflected in National Socialism is in sharp contrast with the Russian concept as reflected in Communism. The importance of religion and philosophy in Oriental groups is in sharp contrast to the importance of economic goods in the American scale of values. The improvidence of

[1] KYRK, Hazel, *op. cit.*, *A Theory of Consumption*, chap. 9.

savages is the other extreme of the emphasis placed upon thrift by that group known as Pennsylvania Dutch. In comparatively recent years there has developed in America a strong group bias for a "decent" burial, which leads to a demand for an amazingly large volume of "burial" insurance, purchased frequently at considerable sacrifice.

These few random samples are perhaps sufficient to illustrate the manner in which group concept of welfare is reflected in the wants of its individual members. In these cases also there is wide opportunity for waste. Group concepts change but slowly if at all, while the economic world in which groups live is tremendously dynamic. A group bias which may have had utilitarian origin may become a false standard of consumption in changing economic conditions.

Social and Governmental Policies. Not only do economic resources, individual inborn tendencies, and group influence affect choice, but so also do social and governmental policies which affect distribution of wealth and income, such as taxation and protective tariffs. While it is true that such policies as these influence consumers' choices and vitally affect their ability to satisfy their wants, no extensive discussion will be attempted here, for they are treated at length in every standard textbook on principles of economics.

In a society where wealth and income are unevenly distributed the very fact of inequality divides consumers into groups or castes according to the size of their incomes. A child reared in the home of wealthy parents will reach maturity with wants quite different from those of a child reared in the home of parents whose income is small. The former child will want things which the latter has never seen and does not know about.

All taxes are ultimately paid out of income, but the American tax system has been built largely on the theory of taxing objects according to ownership, or transactions, or both. Such a system cannot carry to its logical conclusion the principle of taxing according to ability to pay. As a result those incomes most capable of bearing the highest rate of taxation are seldom taxed according to that ability. In fact it is sometimes possible for persons with very large incomes to avoid entirely the obligation of paying an income tax. When a tax on consumption, like a general sales tax, is superimposed upon such a heterogeneous tax system as is found in most states, the burden on that large group of consumers whose incomes are small is still further increased. As a result the area of their wants is still more restricted. It has been estimated that 3 out of every 4 tax dollars represent a reduction in consumption expenditures. A prewar survey shows that sales taxes paid by the average citizen in 39 states amounted to $15 per capita a year. For a family of five this would

total \$75 annually. If this average family of five owned an automobile, gasoline taxes increased the amount by \$27.37 a year, making a total of \$102.37. Another prewar estimate based on all traceable indirect taxes indicated that a family with an \$1,800 income paid \$242.64 in taxes. This was equal to 13.5 per cent of income.[1]

In an effort to find out who pays the taxes the Temporary National Economic Committee had a report prepared showing the ratio of taxes to incomes for ten income classes. The results are summarized in Table I.[2] If these figures are correct they show that from one sixth to more than one third of the incomes of these various groups are absorbed by taxes, leaving the recipients that much less with which to satisfy their economic wants. The advent of Social Security taxes and the heavily increased income tax rate, with the withholding feature, as a wartime revenue measure, cut still more deeply into the purchasing power of consumers and became an increasing factor in affecting consumer choice.

TABLE I.—SAVINGS AND ALL TAXES* AS PERCENTAGE OF CONSUMER INCOME, IN THE FISCAL YEAR 1938–39

Income classes	*Total consumer income (in millions of dollars)*	*Taxes as percentage of income*			*Savings as percentage of income*
		Federal	State and local	Total	
I. Under \$500	2,363	7.9	14.0	21.9	−24.3†
II. \$500 to \$1,000	10,038	6.6	11.4	18.0	− 2.0†
III. \$1,000 to \$1,500	12,280	6.4	10.9	17.3	5.2
IV. \$1,500 to \$2,000	10,210	6.6	11.2	17.8	5.8
V. \$2,000 to \$3,000	12,194	6.4	11.1	17.5	9.6
VI. \$3,000 to \$5,000	7,743	7.0	10.6	17.6	16.8
VII. \$5,000 to \$10,000	4,861	8.4	9.5	17.9	28.4
VIII. \$10,000 to \$15,000	2,238	14.9	10.6	25.5	32.3
IX. \$15,000 to \$20,000	1,601	19.8	11.9	31.7	32.3
X. \$20,000 and over	6,333	27.2	10.6	37.8	38.3
Total	69,861	9.2	11.0	20.2	11.4

* Business taxes were assumed to be shifted to consumers. † Deficits instead of savings.

A protective tariff influences consumer choice either by keeping out of the country goods which people want or might want, or by raising their prices so high as to place them out of reach of the average consumer. In 1943 American buyers of Smyrna figs, Turkish tobacco, and Australian wool bought these products at prices protected by duties of 76 per cent,

[1] *New York Times*, October 29, 1938, based on a survey made by the Northwestern National Life Insurance Company.

[2] Temporary National Economic Committee, *Who Pays the Taxes?* Monograph No. 3, p. 6, United States Government Printing Office, Washington, D. C., 1941.

114 per cent, and 96 per cent *ad valorem*. The *ad valorem* rate on alarm clocks was 123 per cent. Such goods as matches, toothbrushes, and safety razors could be bought only at prices protected by duties of 115, 137, and 39 per cent *ad valorem*. The *ad valorem* duties on scissors, brier pipes, and felt hats were 89, 73, and 98 per cent. Even the baby's nursing bottle could be bought only at a price protected by an *ad valorem* duty of 30 per cent, while the duty on a toy was 104 per cent.[1]

Summary

In the face of limited economic resources consumers with their unlimited wants seek happiness by attempting to satisfy as many wants as possible, or by suppressing some of the wants. Real economic happiness probably lies between the extremes of these two philosophies.

Individual human wants may be classified into nine major divisions, according to origin and nature, while group wants fall into five main fields. Among factors influencing wants are economic resources available, occupational activity, and the group. Influence of the group into which one is born is reflected in goods wanted for survival, prestige, and welfare values. Social and governmental policies such as inequitable taxes and burdensome tariffs affect distribution of wealth and income and thus restrict the range of wants.

QUESTIONS FOR DISCUSSION

1. Are your wants unlimited? Analyze them and expand your views.
2. In the face of crop-control methods and restriction of factory output can we properly speak of the niggardliness of nature?
3. If you have a special interest in psychology make an attempt to outline the psychological origins of your wants.
4. On what basis would you distinguish between wants and needs?
5. Do you think physiological differences in taste are inborn or acquired?
6. Can you add anything to the classification of human wants presented in this chapter?
7. Give an original illustration of the influence of economic resources on human wants.
8. Have you ever engaged in an occupation which required special supplementary equipment?
9. Can you give an illustration of a want influenced by group concept of survival or prestige value?
10. Is there a caste system in the United States?
11. Give an illustration of a specific tariff schedule which influences your economic choice.

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[1] United States Tariff Commission, Letter, June 5, 1943.

12. Are you a taxpayer? Does government fiscal policy influence your economic choices? In what way?
13. Compare the treatment of consumer demand in this chapter with that in your textbook on principles of economics.

PROBLEMS AND PROJECTS

1. List a number of your unsatisfied economic wants; estimate the annual income you would need to satisfy those wants. Do you think you would be happy if you had such an income?

2. Make a list of your most common economic wants, classifying them according to origin.

3. Draw up a list of a dozen commodities and ask ten people at random whether or not they like those things; then ask them to give reasons for their likes or dislikes. Tabulate your results so as to show the various influences back of their wants.

4. Contrast the economic wants of Canadians and Mexicans as you think they are influenced by climate.

5. Compare and contrast the economic wants of five different occupational groups, showing how differences in occupation result in different economic wants.

6. Try to explain why you dislike several things. If, for example, you do not like grapefruit do not consider it sufficient to say that you dislike the flavor; why do you dislike that particular flavor? If you do not like green shirts or hats why do you object to that particular color? Classify the influences back of your dislikes.

3

Who Guides Consumers?

Contrasts between Producing and Consuming. Ancient Athenians had a highly developed art of consuming in contrast with their comparatively primitive methods of producing; modern Americans have a highly developed art of producing in contrast with their comparatively unchanged methods of consuming. It is a striking fact that as society has progressed from primitive to modern methods in producing utilities there has been little increasing progress in the art of consumption. "If a consumption technique were developed as scientific and well organized as our production technique the balance between producing and consuming would be re-established."[1] As producers we have developed to a high degree the principle of specialization, applying it not only to labor but also to the use of capital and land. As consumers we have made practically no use, within the family, of the principle of specialization. While we recognize the advantages of dividing tasks so as to develop inherent and acquired talents, we have not applied that principle to our consuming technique.

With a gradual change from handicraft to factory system of production, the form and location of business organization underwent fundamental changes. The small single enterpriser, operating in his own home with the aid perhaps of members of his family or one or two apprentices, was eventually replaced by the corporation, operating in a separate factory building with the aid of a large number of men, women, and children drawn from most of the homes in the town. While this change was going on, and is in fact still going on, in the producing phase of our life, there has been no comparable change in our consuming activities. In fact the family as a consuming unit has, if anything, become more generalized rather than more specialized. This is because of the widespread tendency for working women and children, as well as men, to go daily from the home as a producing-consuming unit to the factory, which is solely a producing unit. This, of necessity, detracts from the time which any one member of the family can give to consideration of consuming problems. At the same time there has been an increasing tendency for

[1] SHELDON, Roy, and ARENS, E., *Consumer Engineering*, p. 18, Harper & Brothers, New York, 1932.

the incorporated factory to undertake an increasingly large number of tasks formerly carried on within the home, such as baking bread and canning.

A still more significant reason is to be found in the different standards by which each of these units measures the success of its operations. Modern business has one single, definite, measurable test to apply to every transaction. That test is whether or not it will pay. Business is consequently concerned with costs of production and how to reduce them, on the one hand, and with retail prices on the other. The home as a consuming unit has several standards by which to test the success of its operations, but none of these is capable of measurement. We have already proceeded far enough in our analysis of human wants to know that the organic utility of goods is only one of several forces determining consumer choice, and that their contributions to human satisfaction cannot be measured in monetary terms, as can costs of production. This leads us perhaps to the very core of the modern problem of consumer economics. Lacking definite, measurable standards by which to judge the satisfaction which goods and services yield, consumers become easy prey for anyone who does have a definite standard and who has an interest in helping consumers to decide what they want. Present-day consumers are literally overwhelmed with "free" advice as to what they ought to have. There can be no doubt that if the producing phase of our economic life were characterized by anything like the ignorance, lack of purpose, and general haphazardness which characterize our consuming activities Dun and Bradstreet would have to report a much larger number of business failures each year. This is not to suggest that all business firms are free of wasteful inefficiency, but they are much less wasteful than most consumers.

Who Guides Infant Consumers?

The Infant Consumer. Turning from a general discussion such as that in the preceding chapter, of forces playing upon consumer choice, we now have to consider several specific questions. If consumers do not know what they want, if they cannot judge quality nor compare prices, and therefore only partially guide the productive process, we still have to answer the question, "Who does guide production?"

Out of the maze of individual and social wants which beset consumers, they have all been presumed somehow to know what they need and what they want. But what shall we say about that part of our population, comprising nearly one third of it, who are children? Borrowing a legalistic term, they may be described as economic infants. For most of them the matter of choosing goods and services for the satisfaction of

their needs and wants is settled arbitrarily by parents or guardians. An unfortunate few are permitted to have what they want, with the result that weak rather than strong bodies and minds are built. If all children were perfectly free to choose what they want, there can be little doubt that a tremendous increase in demand for candy, ice cream, circuses, thriller movies, and toys would follow, while demand for spinach, carrots, cod-liver oil, public schools, and Sunday schools would drop to the vanishing point.

If the parents of the children are economic adults who know something about utility, and whose choices of goods for their children are based upon a real consideration of their ability to promote welfare, the economic infant consumers will receive a well-balanced provision of food, clothing, shelter, health care, and education which will develop physically strong bodies and alert minds. On the other hand, if the parents themselves are economic infants whose choices of goods for their children are determined by false standards, the children will be permitted to consume what the parents *think* they want in food, clothing, and education, with the result that they will develop physically weak bodies and sluggish minds which will retard individual and group welfare.[1]

While differences in family incomes are important they are not necessarily the deciding factor in determining the relative contribution of consuming standards to welfare. If the family income is so small that it will not buy adequate nutrition, sufficient clothing, and proper housing, not to mention health care and education, it is obvious that the needs of children in such families will not be fully met and that their wants are likely to be distorted. A common criticism of consumers in such circumstances is that they are so ignorant that they would not know how to consume wisely even if they had sufficient income. One can always point to isolated cases of foolish expenditures on the part of families in lower-income groups. If, during the boom period accompanying a war, the money incomes of such people are temporarily increased, it is not surprising that they will demand such commodities as silk shirts and hose, fur coats, and grand pianos. Having been deprived of such things all their lives, it seems quite natural and human that the expenditure of their sudden affluence should be for such comfort and luxury goods rather than for a wider variety of wholesome food, substantial plain clothing, and more adequate housing facilities. If members of other more fortunate groups had a modicum of tolerance they would understand and sympathize with such reactions rather than condemn them out of hand.

This is a situation in which one might well say, Let him who has

[1] HOBSON, J. A., in his *Work and Wealth*, chap. 9, presents a good discussion of this question.

never made a foolish expenditure hurl the first barb of criticism. There has been some evidence already presented and there will be much more to show that some of the most foolish and wasteful consuming standards are to be found among the wealthy. When members of that caste spend four million dollars for a yacht or one hundred thousand for a wedding, instead of being criticized and condemned they are praised and lauded, the expenditure being justified on the pretext that it makes work.

It does not follow that a sufficiency of money income is a guarantee that the income will be consumed wisely. The presumption of course ought to be in that direction, but there is an abundance of evidence available to the intelligent observer that rich parents do not necessarily choose wisely for their children, and that poor parents do not necessarily choose unwisely for their children.

When Does Economic Infancy End? Although there is no evidence to support the belief, it is popularly assumed that children somehow naturally grow into economic adulthood, and as one acquires money of his own to spend, it is presumed that he knows how to spend it wisely. The American educational pattern in the past has included very little if any training for intelligent use of wealth and leisure. Emphasis on production in our economic life has been reflected in our educational process. Chief emphasis has been placed on the study of how to produce and acquire wealth. The purpose of education has been chiefly to prepare children for vocations. The very method used in teaching principles of chemistry and physics, for example, has emphasized their uses in production rather than their possible use by consumers to test the nutritive value of foods, quality of clothing, or wearing capacity of household appliances. While this tendency has been tempered by the development of courses in home economics in high schools and colleges, there are still many children who do not have these facilities or do not use them, and girls rather than boys are largely the ones who receive such training.

When a child reaches a certain youthful age—sixteen years in many states—our compulsory education laws permit him to terminate his formal education and assume his place in the economic world as a producer. As a matter of fact many children assume that role at an earlier age, for part time at least, depending on the school laws of the state in which they live. The fact that a sixteen-year-old boy is able to acquire money by selling his services is no evidence of his ability to exchange it wisely for goods and services. Indeed a man's ability to acquire an annual income in excess of one million dollars is no evidence of his ability to dispose wisely of that enormous claim on wealth. Qualities which one must develop to acquire wealth are quite different from, and frequently alien to, the qualities necessary for its wise utilization. Numerous illus-

trations might be given of millionaires whose endowment of foundations and institutions for the advancement of pet hobbies stands as mute evidence of their childishness as consumers.

This leads to the conclusion that for some people economic infancy never ends. Like the legal fiction that an infant suddenly blossoms into maturity necessary for assumption of the duties and obligations of citizenship on his twenty-first birthday, the economic fiction that an infant gradually and without guidance develops into maturity qualifying him to assume the full duties and obligations of a consumer, is simply without foundation.

Obviously a person's actual training partially determines the answer to the question of when his economic infancy will end. If he has been reared by parents who themselves are still economic infants there is no good reason to suppose that he has developed or will develop the characteristics of an economic adult. On the other hand, if he has been reared by parents who have reached some degree of maturity as consumers there is reason to believe or hope that he has developed or will develop the qualities essential to what may well be called consumer citizenship.

As a result of our national emphasis on the acquisition of more income as the way to economic welfare, there is practically no adult consumer education in the United States. There are a few agencies breaking ground in that direction, whose activities will be described in Chapter 15. But the process of teaching old consumers new tricks is a difficult one. Since man is so largely a bundle of instincts and habits, his consuming standards are so definitely fixed by the time he becomes an adult that he has little or no interest in trying to learn new ways of living. The living process appears to be so simple that many adults resent the idea that anyone else can tell them how to live more wisely. Moreover, it takes time to perform intelligently the functions of a consumer. In the past men and women have been so preoccupied with the struggle of earning an income that they have had no surplus energy or leisure to devote to improvement of their living standard. Perhaps present trends toward shorter hours in industry, in most cases with no more, or even less, total income, will provide the necessary leisure and stimulus to impel adult consumers to learn more about the qualitites of "buymanship." The future also presents to labor unions an opportunity which has been largely overlooked in the past, to broaden the scope of their activities beyond the functions of bargaining and providing insurance benefits, to include the important and expanding field of consumer education.

Lack of adult consumer education has resulted in consumers drifting along, learning by experience, and paying producers dearly for the privilege. If economic infancy actually ended for all people at some

determinable time, consumers would then more nearly know what things are best for them and would want those things. The possibilities of such an achievement present a striking challenge to the imagination, as one illustration will show. Dr. James S. McLester, past president of the American Medical Association, believes that the key to man's control over his destiny and power to evolve a race of supermen is to be found in intelligent and adequate nutrition. Said he, "Man's place in future history will depend in no small degree on the food he eats." During the past twenty years medical science has experimented with controlled nutrition for animals so successfully that under certain circumstances their length of life can be extended and the species improved. Undernourished children suffer more in the growth of their transverse than of their longitudinal dimensions. Their long bones continue to grow faster than other parts, resulting in a thin individual with sunken chest and gaunt appearance.[1]

There is much evidence to show that outdoor camp or army life in which diet is controlled by persons trained as dietitians invariably builds better bodies. There can be no doubt that a communal form of living in which every person received the supply of food necessary to meet physical requirements as determined and prepared by trained dietitians would result in a physically superior race. This would be accomplished, however, at the expense of our highly prized freedom to choose and consume according to our own ideas of what we want. While there is no likelihood that as a group we shall ever be placed under such disciplinary control, each of us as an individual must face squarely the fundamental issue raised. That issue is whether the freedom of choice we enjoy is worth the price we pay for it in terms of poor health and incomplete living.

Who Guides Parent Consumers?

Producers Make Every Possible Effort. From the status of economic infants whose consumption has been guided by parents, themselves lacking adequate training, it is but a short and easy step to fall into the practice of letting producers guide one's choices. Producers are not only willing, but make every possible effort so to guide consumers' wants as to

[1] *New York Times*, June 12, 1935; for additional information concerning the relation of nutrition to consumer welfare see *Journal of Living*, July, 1941; also the papers read at the National Nutrition Conference held in Washington, D. C., in May, 1941, especially Sherman, Henry C., *Adequate Nutrition and Human Welfare;* Murlin, John R., *Nutrition in the First World War and Now;* Wilder, Russel M., *Mobilizing for Better Nutrition;* Elliott, Harriet, *Nutrition and Consumer Protection in Defense;* Hershey, Lewis B., *Selective Service and its Relation to Nutrition;* Wallace, Henry A., *Nutrition and National Defense;* McNutt, Paul V., *The Challenge of Nutrition.*

benefit themselves. Herein lies the clue to the change which has taken place to a large extent in modern life in the control of our economic system. With the advent of machines and division of labor the economies of producing on a large scale could be realized only by steady maximum production. Producers could not let expensive equipment stand idle while waiting for orders, so the practice of producing goods in anticipation of demand for them began. Then as output increased, producers could not afford to let inventories accumulate while waiting for consumers to clear the shelves. Consumers failing to respond sufficiently to the lure of lower prices, which were attributed to economies of large-scale production, were besieged by aggressive sellers entrusted with the task of creating demand. Thus came the advent of modern advertising and salesmanship in all their variant forms, together with their handmaiden, installment buying. Consumers had proved so thoroughly incapable of guiding producers, and so highly susceptible to suggestions from sellers, that the sellers now play a large part in determining the choices of parents for themselves and for their children.

An interesting analogy between the theory of political control and the theory of economic control has been drawn. According to political theory citizens select their government officials and thus control government and governmental policies. In fact, however, political bosses long ago learned to control the political machine and to manipulate it so as to benefit themselves. It is only in comparatively recent times that producers have discovered the technique which makes it possible for them so to control consumer demand as to benefit themselves.[1]

Producer Selling Technique. While buying and consuming as carried on by consumers are arts, not sciences, producers have gone far in reducing the art of selling to a science. The science of psychology has become the tool of the salesman. There is no instinct of which he does not try to take all possible advantage. From the tender love of a mother for her child to the pugnacious carry-over from our primitive ancestry, appeal has been made to every one of the known inborn tendencies. Vanity and the desire to attract attention through conspicuous consuming are used. The desire to be up to date is played upon. Imitativeness is made to pay. The deep-seated power of custom is turned to advantage. The very ignorance of consumers is turned to profit through price appeal. Smartness of avoiding obsolescence is brought down to lower-income groups by means of installment selling, making it easy to buy when it is unnecessary. For the sake of profit, consumers are appealed to in the names of religion, patriotism, state and local pride, and group loyalty.

[1] Kyrk, Hazel, *A Theory of Consumption*, chap. 5, Houghton Mifflin Company, Boston, 1923.

Profit and Loss Statement. If consumers do not guide producers it is pertinent to ask what does. On what basis do producers decide what to produce, and how much? How do they determine what standards of quality to observe? How do they detect the passing of old wants? How do they discover the existence of new wants? Answers to these questions are to be found in the driving force which motivates modern business. To the extent that producers do guide production the single test which they apply is that of profit. To the extent that consumers fail in their function of expressing their choices in the market place, producers are governed by the profit and loss statement.

Herein lies the heart of the modern economic problem. The only guide which consumers have is utility, which is subjective and incapable of measurement. The producers' primary guide, on the other hand, is profit. If diluted kerosene can be sold as an insecticide at several hundred per cent profit, it will be sold even though it is not good for that purpose or is overpriced. The profit and loss statement is definite, clear, and objective. Since the purpose of business in a capitalist economy is to make profit, if the consumer does not know what he wants the producer stands ready and eager to tell him what the producer wants him to have, which is whatever will yield the most profit.

Consumers' Counts Against the Profit System. The basic assumption of the profit system is that it will pay producers to offer for sale only those things which consumers want, which in turn is predicated on the assumption that consumers know what they want. In fact, these assumptions fail in at least three respects.

In the first place the desire for profit supersedes the service motive. That is to say, producers frequently find it more profitable to produce goods intended for sale rather than those intended for the service of consumers. Profits flourish in an economy of scarcity rather than in an economy of abundance. From a producer point of view scarcity results in high prices and greater profits; from a consumer point of view utility is increased by having an abundance or goods and services at low prices.[1] This leads to the fact that producers may actually realize greater profits by performing no service at all or even by performing a disservice to consumers. The spectacle of producers deliberately restricting the output of factories, farms, and mines is to be explained only by the fact that in so doing they receive or expect to receive greater profits than by increasing the volume of goods offered for sale. Recent surveys of America's

[1] For an elaboration of this point see BOWMAN, Mary Jean, and BACH, George Leland, *Economic Analysis and Public Policy*, chap. 13, Prentice-Hall, Inc., New York, 1943.

consuming capacity demonstrate beyond question the ability of the nation's 136,000,000 consumers to use much more food, clothing, shelter, health care, education, and recreation than producers find it profitable to supply. As a result producers deliberately restrict the acreage planted to such agricultural products as wheat and cotton, or destroy surpluses already produced. It is not uncommon for producers to dump coffee and bananas into the ocean for the purpose of creating an artificial scarcity designed to maintain prices high enough to yield profits.

A second consumer objection to the profit system is that it causes producers to attempt to control consumer demand and to guide it into those channels which will prove most profitable to producers rather than most beneficial to consumers. This leads to the expenditure of tremendous amounts of wealth and the use of much human effort in such activities as advertising and salesmanship. The purpose of these activities is not primarily to help consumers find the goods and services they want, but rather to force them to buy the particular goods and the specific brands which will yield the greatest profit to producers. This results in a large volume of competitive waste. Consumers are implored, exhorted, and even commanded to consume more wheat products. If they obey, producers of other commodities, say raisins for example, find their sales diminishing and double their advertising budget to implore, exhort, and command consumers to eat more raisins. Manufacturers of a branded cigarette urged consumers at one time to "reach for" their cigarette "instead of a sweet"; and manufacturers of candy retaliated by advising consumers to smoke less and eat more candy, and also went into court to prevent cigarette advertisers from encroaching on their preserves. As a result of such competitive pressure it is no wonder that consumers become thoroughly bewildered.

A third indictment of the profit system by consumers is that the desire for profit is so strong that it leads some producers to resort to any means which are likely to yield a profit. In colonial days it was more difficult for a producer to perpetrate a fraud on consumers, because the market was so limited that once the fraud was detected or had been worked to its limit its profit-yielding possibilities were ended. Today producers have 136,000,000 possibilities. They need not concern themselves about developing repeat sales. In such an extensive market a fortune may be made before a fraud can be detected. As a result of this situation some modern producers find it highly profitable to resort to such practices as misbranding, mislabeling, adulteration, and untruthful advertising. Some of them will do anything to get a dollar. In January, 1942, a shipment of sirup from Chicago to Detroit was seized by officials of the United States Food and Drug Administration. The product

was labeled "Click Waffle & Pancake Syrup. Content 11 Fl. Oz. Contains Cane and Maple Syrups." The article was alleged to be adulterated since an artificially flavored and artificially colored substance containing glucose had been substituted for cane and maple sirups. The product was alleged also to be misbranded because the statements on the label were false and misleading, because the product was an imitation of another food, and because it was short volume. Although the shipper of the product was known, he did not appear to defend the case, so a judgment of condemnation was entered and the product was ordered destroyed.[1]

A typical issue of *Notices of Judgment* contains from 200 to 225 similar cases. For example, the issue for May, 1943, reported 200 cases, 49 of which dealt with adulteration and misbranding of fruits and vegetables, and 40 with dairy products, chiefly butter and cheese. Of the remaining cases 29 dealt with saccharine products, mostly candy, 16 with fisheries products, 11 with fats and oils, 11 with cereal products, the others being scattered among poultry, nuts and nut products, and miscellaneous items.[2] These are by no means all of the cases in which, in that month, producers resorted to such means to get a profit. These are only the cases which were detected and which involved interstate commerce. No one knows, no one can even estimate, the extent of such practices in modern business.

In so far as producers succeed in their efforts, the process of controlling and guiding the economic system is reversed. Consumers do not buy; rather, producers sell. An exponent of the new art of so-called consumer engineering says, "Strange as it may seem, a definite program for adapting goods to the needs and desires of the people who buy them is a comparatively new thing. In the early days *the manufacturer decided* what he would make, what color or design, how large the unit of quantity, every detail. There it was. *The consumer could take it or leave it.*"[3]

Do Producers Produce What Consumers Want?

Producers Attempt to Anticipate Consumer Demand. The presumption has been that the profit motive will lead producers to supply consumers with the things they want. But evidence has been presented, and much more is available, to demonstrate that what it pays producers to produce is not necessarily what consumers want or need. This is especially true since consumers as a group are so susceptible to producers' efforts to

[1] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act,* March, 1943, No. 3641, p. 188.

[2] *Ibid.,* Cases 3651–3850.

[3] Calkins, Earnest Elmo, pp. 5, 6 in Sheldon, Roy, and Arens, E., *Consumer Engineering,* Harper & Brothers, New York, 1932. Italics supplied.

control them. Under these circumstances it is pertinent to inquire whether producers actually do offer in the market place all the goods and services which consumers want and only those which they want. Are there goods produced which consumers do not want? Do producers ever offer for sale goods and services which consumers do not need? Answers to these questions are rather clearly suggested by evidence already presented.

It might well be contended, and probably most economists would so contend, that the very fact that products offered for sale are bought by consumers is *prima facie* evidence that those are the things they want. If consumers do not buy them the producer incurs a loss and is thus discouraged from further attempts to market such goods. On the other hand, if consumers buy the goods and producers make profits they are thereby encouraged to offer more of the same or similar products for sale. If all the implied assumptions involved in this contention had a basis in fact we might then accept this view. But enough evidence has already been given, and more will be presented, to cast a considerable shadow of doubt on the validity of the basic assumptions.

In seeking the answers to these questions it must be remembered, also, that under our modern system most goods are produced in anticipation of demand rather than after a want has been felt by the consumer and registered in the market place as a demand for a specific product or service. If all producers waited until consumers had registered their choices, as is done under the system of producing what are called custom-made goods, it might then be said that producers produce what consumers want.

Why Not Produce to Order? There are at least two basic reasons why this method of production is not more widely followed in the United States. First is the argument presented by producers that they cannot realize the economies of large-scale production if they wait for consumers to express their demands. In order to keep their large plants constantly operating they must estimate what consumers want and how much, then produce those goods, and finally use all possible means to make consumers think that those are the goods they want. The business cycle with its periodic depressions, resulting in partial or complete cessation of the productive process, causes the very losses of large-scale economies which producers are seeking to avoid. Why is it not possible, then, to reconstruct the sequence of cause and effect by getting consumers to express their wants in advance? If this could be accomplished, not only would the original assumption be true, that goods produced are those which consumers want, but also a long step would be taken toward regularization cf the productive process and elimination of business cycles.

If two such beneficial results might follow such a change in the productive process, why do not consumers realize them by expressing their choices far enough in advance in the form of orders so that producers may operate their factories, farms, and mines regularly, knowing that what they are producing will be sold at a profit because the order is already placed?

Answers to this question constitute a second reason why a system of producing to order does not prevail in the United States. There are a number of answers, of which perhaps the most basic is the inertia of consumers. Whether this is a human tendency which cannot be overcome, or whether it is a result of generations nurtured in a system under which planning for the future has been done by producers, it is difficult to say. The fact of the situation is that very few consumers anticipate their own wants. They live from day to day with scarcely more thought of their future needs than characterizes primitive people. Even in those cases where consumers know that they will be wanting coal for winter months, and new clothing in the spring, they do not express their wants to the producer in advance. Suddenly when the need becomes pressing they expect to find coal ready for immediate delivery, and clothing already made to fit their particular angles and curves.

Even if consumers could be educated to register their wants in advance there would still be production problems created by those who ordered goods only to change their minds and refuse to accept delivery. Still other difficulties would be encountered in the risks and uncertainties of the productive process itself. What would happen if a clothing manufacturer or an automobile producer, having orders for a large number of suits or cars, should be prevented from making them by an interruption caused by fire or other natural hazards or by labor difficulties? What would happen to the cotton and wheat farmers who had planted a definite number of acres, in response to orders placed, if the crop failed or proved inadequate due to drought, or hail, or some other natural hazard over which they had no control?

The Present System Yields Practically All Consumers Want and Much They Do Not Want. Reverting now to one of the original questions as to whether or not there are things we want which are not produced, an answer can be given in the light of the foregoing discussion of the method by which most of our goods are produced. Under the system of production in anticipation of demand, motivated by the desire for profit, it is unlikely that producers would fail to produce anything which consumers might possibly want. During recent years when students have been asked whether or not there is anything they want which producers do not produce they have found it difficult to think of a single thing. In most

cases such things as are wanted but not available on the market can be secured if the consumer is willing to place an order and able to pay the price to cover its cost.

The real difficulty into which the present system leads consumers is that it produces many things they do not want and then puts pressure on them to buy. It has been assumed in the past that if a product is produced consumers will buy if they want it and the producer will reap the profit, but if consumers do not buy the producer will incur a loss and produce no more. What actually happens is that instead of accepting the consumers' judgment that they do not want the goods, modern producers, in order to avoid loss, set out to compel consumers to buy the goods, using whatever methods will yield the desired result. In the words of two such persuaders, this newly developed art which is called consumer engineering "is the science of finding customers, and it involves the making of customers when the findings are slim."[1]

Source of Waste. This confused situation with its false guidance leads to an appalling amount of waste. From the consumer point of view waste results the moment any other test than utility determines the nature of things consumed. As soon as the conventional factor and the producer's quest for profit supplant consumer utility as a guide to production, waste replaces economy and utility.

Summary

Guided by measurable profits, producers have inaugurated extensive changes in organization and methods calculated to increase efficiency. Consumers, with no other guide than unmeasurable utility, still center consumption about the family, whose form and methods have changed but little in spite of sweeping changes in production. Economic choice for infant consumers is determined largely by parents, themselves too often infants as consumers. This makes possible partial control of human wants by producers, enabling them to concentrate on producing what will pay most profit rather than what may promote human welfare. Distortion follows, leading to false standards, fraud, and deceit. As a result producers offer for sale many things consumers do not want, while there is a dearth of genuine wealth which consumers need.

QUESTIONS FOR DISCUSSION

1. Can the principle of specialization be applied in family consuming activities?
2. Do all rich people spend their incomes wisely?

[1] Calkins, E. E., in Sheldon and Arens, *Consumer Engineering*, p. 19, Harper & Brothers, New York.

3. Contrast the qualities you think are important for acquiring wealth with those necessary for its wise use.
4. Classify yourself, members of your family, and your intimate friends as economic infants or adults.
5. Which do you prize more highly, your health or your freedom to choose and consume whatever you wish?
6. Do you appreciate or resent being told how you might improve your consuming practices?
7. Who, would you say, guides or influences your parents in their economic choices?
8. Can it be said fairly that advertising and selling techniques are designed to force consumers to buy rather than to help them make the best decision?
9. If a system of producing to order were substituted for production in anticipation of demand, what would be your responsibilities? Would you meet them?
10. According to this chapter, who controls and guides our production system? How does this answer compare with that in your textbook on principles of economics?

PROBLEMS AND PROJECTS

1. Write a short summary of the specific training you have had in spending money. Do you think you are a good buyer?

2. Interview ten housewives, asking each what experience as a buyer she had before her marriage; secure also information concerning their purchasing methods. This project may be varied by having each class member secure information from his or her mother, and then combining the results in one report.

3. Make a study of the curriculum in your high school and college to discover what consumer education is provided. What proportion of the total course offerings is devoted to consumer education? To what extent is consumer training given in such studies as chemistry, physics, zoology, botany?

4. Collect some examples, in your own vicinity, of producers destroying "surplus" stocks of goods in order to raise prices.

Part Two

RESTRICTIONS ON CONSUMER CONTROL: FORCES BACK OF CONSUMER DEMAND

4

Freedom of Choice

The Consumer's Formal Freedom of Choice

What Is Freedom of Choice? Two basic facts from which any study of economics must proceed are the insatiability of human wants and the scarcity of means for satisfying those wants. Whether we know it or not, as groups of individuals we organize some kind of system whose ostensible purpose is so to use scarce means of production as to secure maximum satisfaction of wants.

Historically, society has resorted to several different forms of economic organization. In a primitive stage of development man's organization for satisfying his wants was simple and direct. It has been described as a system of direct appropriation, from nature, of things wanted by man. Hunting and fishing with a minimum of equipment characterized that stage of development. The range of human wants was limited, yet the organization for satisfying them was so inadequate that all wants could not be satisfied. Consumers in such a system had very little freedom in choosing the things they wanted.

The second major development in forms of economic organization has been called the pastoral stage, characterized by the beginning of domestication of animals and group use of land for grazing. That system opened to consumers new wants and new means of satisfying them.

It was a logical and easy transition from the pastoral to the agricultural stage of economic organization. That development marked the beginning of private ownership of land and the emergence of the individual. With the further domestication of animals, the planting of cereal crops, and the establishment of permanent abodes the area of human wants was broadened. Individual in contrast with group wants for the

first time became an effective means of determining what should be produced.

The stage of development known as the handicraft period marked the beginning of man's ability to fabricate basic materials so as to yield greater utility. The development of towns and the payment of wages in money, together with the beginning of a tendency toward specialization in production, gave to consumers an apparently greater freedom in choosing the things they wanted.

These developments have been carried to their logical conclusion in the present economic system. In that stage of economic organization variously described as the industrial period, machine age, or capitalistic system, extreme specialization in specific tasks for the performance of which the individuals receive money wages, makes it necessary for each one to exercise considerable choice in disposing of his money wages. Specialization and the machine age have resulted also in the creation of many new devices for satisfying human wants. As a result writers on economic questions usually agree that the modern consumer has greater freedom in choosing those economic goods and services which he wants than his ancestors ever knew.

Formal freedom of choice, then, is the power of consumers in an economic system characterized by scarcity and governed by a price system to choose those goods and services which they want. This presumes of course that consumers know what they want and carries an appearance of democracy in consumption which is not altogether real. In comparing political and economic democracy the point has been stressed that every citizen has one vote in political life and that every dollar which he owns is the equivalent of one vote in his economic life. The analogy does not hold, for wealth and income are so unequally divided that those having the greatest number of dollars by that very fact have the greatest number of votes. The net result of this situation is that while a few consumers have a wide field of choice, most of them are narrowly restricted. What is even more serious is the fact that those with the largest number of dollar votes are able to order the production of "illth" (goods which retard rather than promote human welfare) or "nealth" (goods which neither promote nor retard human welfare) before others have a sufficiency of wealth (goods which promote human welfare). Yet as long as human wants exceed the scarce means of satisfying them some system of proportioning is necessary.

If the goods produced are not to go to those best able to pay for them, to whom shall they go? If producers are not to produce comforts and luxuries for those able to pay, what shall they produce? In a profit economy the price system is a simple, effective device for regulating the

character and volume of production. True, it is impersonal and may sacrifice the welfare of many to the whims of a few, but defendants of the present system may honestly inquire what other system of control is possible. Formal freedom of choice may work badly, but it works. Can any other device guide production more effectively? That is to say, can any other system more nearly achieve the goal of human welfare?

Authoritative Control

Formal Freedom of Choice Is Not Universal. While consumers as a whole are limited in their formal freedom of choice by the availability of goods and the size of their money incomes, some consumers have little or no freedom, and all are limited on certain occasions by special circumstances. Children, comprising nearly one third of the national population, have very little if any freedom of choice. Their parents or guardians exercise an authoritative control on their behalf. This control is presumably determined on the basis of welfare. The outstanding illustration of exercise of authoritative control is to be found in our system of compulsory education, which requires every child up to a certain age to accept an economic service which the state thinks will promote his welfare. The individual has no choice in this matter. Others in the same category of persons whose economic wants are determined by someone else, include inmates of almshouses, prisons, and reformatories. To a slightly less degree the economic wants of soldiers are determined by those in authority. These consumers living in a price system are denied that freedom of choice which is one of the most important justifications for its continuance.

Even economic adults are denied full freedom of choice in a price-governed economic system in times of extreme emergency such as war. Once a nation finds itself embroiled in an armed conflict it usually succeeds in securing practically unanimous support of its citizens. In modern warfare this includes economic as well as military activities. Faced with fear of conquest by a foreign foe, the people of a country rally together, regardless of right or wrong, to support their military leaders and to conserve their scarce economic resources. This means, as in the United States during World War II, that authoritative control for apportionment of scarce materials is vested in certain political or military leaders. The extent to which people will thus give up formal freedom of choice depends in large measure on their judgment of the seriousness of the conflict. That in turn is quite largely under the control of government censors whose powers deprive the press of freedom of choice in disseminating news and constitute authoritative control in rendering news service.

While it has always been true that economic strength underlies military strength, that truth is somewhat more obvious in modern warfare, which, like the economic system itself, has become highly specialized with the various parts mutually interdependent. Food for soldiers is as important as munitions or their weapons. Shoes, clothing, hospitals, ships, are only a few of the basic necessities for modern warfare. In the United States during World War II men between the ages of 18 and 38 were drafted for military service, and men up to age 65 were registered under the Selective Service Act. Some may not have wished to leave their country to fight on foreign soil. They might have preferred to remain at home with their families, doing work to which they were accustomed and which they enjoyed, but they had no choice in the matter. The War Production Board, the Office of Price Administration, the National War Labor Board, the War Manpower Commission, the Office of Economic Stabilization, the Office of Defense Transportation, the War Shipping Administration, the Petroleum Administration for War, and the Office of Civilian Defense are some of the more important agencies which exercised a measure of authoritative control over economic resources of the nation during that period. So far as possible, consumers were cajoled into accepting certain restrictions voluntarily, but when such a method failed to conserve the supply, positive measures of control were invoked. Thus on the one hand consumers were urged to restrict their traveling on railroads, busses, and airlines, while on the other hand they were definitely rationed on automobile tires, gasoline, and many foods.

Under these circumstances the objective of achieving human welfare gives way to the objective of winning a war. Economic resources, human life, nothing matters except winning the war. The purposes of authoritative control are to prevent all possible wastes of wealth and to direct the use of all wealth into one main channel supporting the war machine.

Another case in which economic control through the price system gives way to authoritative control and apportionment of resources is found in the wake of natural catastrophe. When many people in any section of the country are the victims of fire, flood, drought, tornado, earthquake, or other natural hazard, the suddenly restricted supply of economic goods and services is apportioned through authoritative control. To permit apportionment in the usual way through the price system would create what all would admit to be an intolerable condition. In such a time the impersonality and inequity of the price system stand out in bold relief. To permit the fortunate few whose entire possessions were not destroyed to buy all the limited supply of food, leaving those who had been completely dispossessed to starve, is the very

thing which authoritative control is designed to avoid. Yet this sort of thing goes on daily in normal times. Having become a commonplace it fails to attract public attention and popular fancy as easily as the more spectacular, though frequently less serious, natural catastrophes.

Still another type of catastrophe which seriously restricts freedom of choice is that feature of the modern economic organization which we call depression. In the minds of some this should be included as a natural catastrophe over which man has no control, but the modern view holds that it can be controlled and even prevented by proper exercise of man's intelligence. Basically, it is this very freedom of choice in producing and consuming which leads to cyclical fluctuations in economic life. It is not necessary to carry this suggestion further, for the literature of economics abundantly reflects the thinking of both schools of thought. What is significant for our purpose is the fact that when a depression occurs millions of consumers are deprived of part or all of their purchasing power and thus denied freedom of economic choice. When a system of public relief is instituted, restrictions on freedom of choice continue. When relief takes the form of food, clothing, and housing, consumers are compelled to accept what the relief authorities place at their disposal, even though it may be inadequate. It is the result of authoritative control. In those cases where relief takes the form of cash, the consumers' freedom of choice is limited not only by the amount of money thus placed at their disposal but also by formal and informal restrictions on the manner in which it may be spent. Relief authorities in particular, and the public in general, are extremely critical of what they call wasteful expenditures on the part of relief recipients. Any tendency on the part of the latter to indulge in freedom of choice is likely to bring not only public censure but actual interference by administrative officials holding the power of authoritative control. Formal freedom of choice, during a depression, thus becomes a luxury for a few rather than reality for the masses.

A fundamental difference between this case and the two preceding should be noted. In the other cases authoritative control grows out of fear of a commonly recognized enemy in a war, and fear of a scarcity of economic resources after a wholesale destruction of wealth by natural catastrophe. In the case of depressions, however, while there is a recognizable common enemy it is invisible and elusive, and the fear of scarcity is the result not of destruction but of failure to produce. It is a striking commentary on the group mind that the more obvious though less serious catastrophe more easily wins united opposition than the less obvious, though, from the standpoint of human welfare, more serious catastrophe. This observation leads to the conclusion that authoritative

control over the apportionment of economic resources is likely to succeed only in those exceptional circumstances where a greater primary social need is recognized and accepted by the group, coupled with a fear that economic resources may be inadequate to meet group needs.

Freedom of Choice under Socialism. Between the extremes of absolute freedom of choice on the one hand and absolute authoritative control on the other, there are forms of organizing economic life which rely on a combination of these forces to secure that apportionment of resources which will promote human welfare. Before discussing the form called socialism, let us first consider the fact that capitalism does not permit absolute freedom of choice. In addition to the restrictions already considered there are others. For the sake of group welfare individual consumers are restricted in the type of house they may construct, in the way they may drive their automobiles, and in the amount of liquor they may consume. In congested urban centers the construction of frame houses is forbidden. Driving an automobile at excessive rates of speed or while under the influence of intoxicants is prohibited. The consumer who overloads with liquor may be jailed till he recovers his equilibrium. There are numerous such restrictions but it is significant to note that for the most part they are negative. Much more emphasis is placed upon telling consumers what they may not do than upon telling them what they should do. This system of restrictions for the protection of consumers finds even wider expression in numerous laws which seek to prevent producers from offering goods and services detrimental to human welfare.

That form of economic organization called socialism carries established means of authoritative control much farther. The socialist idea is to have the socially necessary means of production collectively owned and controlled through the medium of the state. Production for use would displace production for profit. Under this system would consumers have more or less freedom of choice? Would the price system be retained, or would it be displaced by some other means of guiding production? The forms of socialism are so numerous and varied that it is difficult to answer these questions definitely. Under that system described as state socialism the first significant change from the present system would be collective instead of private ownership of the basic means of production. Under this collective ownership the motive for producing would be that of creating goods and services for the satisfaction of human wants rather than their production for the primary or sole purpose of making profits. Unless the price system were retained, state officials would have to assume responsibility for deciding what

should be produced and how much. Consumers' freedom of choice would then be restricted within the limits of goods available. But no such program of complete control is included in the socialist program. The price system would be retained, and consumers might thus continue to have as much freedom of choice as at present. Indeed they might even have more, for if the supply of some goods demanded should prove insufficient, prices would rise and state managers would thus be encouraged to increase the supply just as private managers are under the present system. Conversely, if state managers of collective industries offered goods which people did not want, their prices would fall and the managers would know that consumers did not want them. Freedom of choice might actually be extended, since production of goods for use instead of profit would reduce or eliminate the waste of economic resources in the production of illth and nealth (page 52), and release them for the production of wealth. This would amount to an actual increase in the supply of productive factors, with a consequent lowering of costs of producing staple commodities on a large scale.

A second significant respect in which socialism would differ from the present system would be its emphasis on reduction of inequality in the distribution of wealth and income. It is not necessary to discuss the means by which such a goal might be achieved or the probability of its success; but if it were achieved the area of free choice would be considerably extended. Consumers whose incomes are now so small that their freedom of choice is largely negative would have more purchasing power, with a surplus above their own needs to permit the acquisition of commodities commonly known as comforts.

There is no magic about socialism which would suddenly create economic men. There is no reason to believe that consumers would be any wiser under that system than under the present one. The chief difference would lie in the fact that whereas producers now seek to influence consumers to purchase that which will yield a profit, social producers presumably would seek to influence consumers to purchase those goods which would yield most in real utility. This assumes not only that social producers would have a different motivation, but that they would also have superior technical knowledge. The extent to which one accepts these assumptions is a measure of one's belief in the probable success of a socialist program.

Freedom of Choice under Co-operation. The co-operative movement, for promoting the welfare of consumers, operates within the framework of capitalism. Each co-operative organization of consumers usually begins in the field of merchandising and if successful extends back into the processes of manufacturing. The central purpose is to secure co-

operative manufacturing and merchandising of those goods and services which organized consumers want. Originating, as it usually does, among workers with small incomes, its operation is largely confined to the production and sale of essential products. The chief distinction between the co-operative movement and the present system of production is found in the extent to which democratic control prevails. The corporate form of organization which dominates production at present permits concentrated control by a few for their own profit. In co-operative organizations the device of giving each member only one vote, regardless of the amount of capital invested, permits democratic control; and since consumers are the ones in authority the presumption is that they will vote only for the production of goods they want. Thus by following the motive of production for use instead of production for profit the output of illth and nealth should be reduced or eliminated.

Operating as it does within the framework of capitalism, the co-operative movement of necessity retains the price system. In fact, the practice is to charge consumers prevailing market prices, but to distribute profits, or savings, to the members of the organization on the basis of their patronage rather than the amounts of their investments. In this way larger consumers benefit and the central purpose of any economic organization, which is satisfaction of human wants, is emphasized. To the extent that this method increases the real income of consumers their freedom of choice is extended. Since, however, consumers themselves are the ones who decide what shall be produced and how much, there is no assurance that they will show any greater wisdom. The presumption is in that direction, however, since they are free from the powerful influence of producers primarily concerned with their own welfare rather than that of consumers.[1]

Freedom of Choice under Fascism. Consumers in a number of countries, notably Germany and Italy, have witnessed the evolution of a politico-economic form of organization known as fascism. Under this form of organization the state joins forces with a small group of property owners with the ultimate effect of strengthening their economic position at the expense of the masses of worker-consumers. Extensive political and economic power is vested in one individual commonly described as a dictator, whose policies and acts reflect the wishes of the small but powerful group which maintains him in his position and to whose wishes he responds. The price system is retained under fascism, but through monopolistic or semimonopolistic organization its free operation is restricted. In contrast with socialism, the basically necessary means of

[1] The co-operative movement in the United States is discussed further in Chapters 18 and 19.

production are privately owned and controlled for the profit of fascist owners, and also for the benefit of the fascist state as ordered by the dictator. Consumers find their freedom of choice severely restricted. Not only are the food they eat and the clothing they wear largely determined by state officials, but the things they read and the thoughts they think are products of authoritative control. The apparent purpose and justification of fascism is to create a powerful military state in the professed belief that by such means the welfare of its citizens will be promoted.

Freedom of Choice under Communism. Strikingly similar to fascism in its methods but fundamentally different in its purposes is that form of politico-economic organization known as communism. As an economic ideal the purpose of communism is so to organize economic life that each member of the group will contribute services to the extent of his ability, receiving in return goods and services according to his needs. The first half of this formula is in harmony with the capitalist theory, but the second half is very different from it. While productivity is measurable in the market place, though with nothing like the precision frequently claimed for it, individual needs are incapable of monetary measurement. Being subjective, they vary with individuals. What are the needs, for instance, of a scientific investigator? Is his request for comfortable living quarters and pleasurable entertainment justified? What are the needs of a farm hand in comparison with the needs of a factory worker? Who is to decide these questions? These are typical of the difficult problems which proponents of communism must face. The communist purpose is to divide scarce goods and services among all members of the group according to their needs before anyone has the right to comforts or luxuries. This automatically eliminates freedom of choice. It requires the substitution of authoritative control by someone. That authority must have the power and should have the wisdom to distinguish between needs and comforts. In a completely communist organization there would be no price system, goods and services being apportioned according to the dictates of an official. A consumer might want a new pair of shoes, but if the proper administrative official ruled that he did not need them as much as other consumers he would be compelled to go without them.

The ostensible purpose of communism is to promote welfare by insisting upon the satisfaction of all basic human wants prior to the satisfaction of any secondary wants. The substitution of authoritative control for the price system assumes that there are individuals with sufficient wisdom and impartiality so to guide the productive process that the central purpose would be realized.

In Which Direction Does Welfare Lie? It is difficult to advance a rational answer to this question. While we have had experience with freedom of choice and may realize how badly it functions at times, we have had very little experience with genuine authoritative control. This leaves us with no adequate basis for comparison. The limited experience of the United States with wartime control has been characterized by much chafing and dissatisfaction. But it is remarkable that there was not still more criticism, when one considers the precipitate haste with which a nation of consumers was pushed from one system to the other.

Turning to other countries, we find little helpful experience to serve as a guide. Such knowledge as we have of the operation of fascism would scarcely lead consumers to seek that form of control as a substitute for freedom of choice. Even though one may choose badly there is some satisfaction in being able to choose. There is no completely socialist or communist group upon whose experience we can draw. Though commonly described as communist, the Russian system is a combination of socialism and communism from which it is difficult to draw helpful conclusions. While there is a large degree of authoritative control in Russia, a modified price system is retained. To the extent that Russian consumers have money with which to buy goods in an open market they have freedom of choice. Perhaps if a generation of consumers were reared under authoritative control and never knew the experience of free choice, such a system might succeed. People are to so large an extent creatures of habit and custom that if the habit of accepting what someone else decided was once firmly inculcated, consumers might continue to accept the choices made by others without question. From a purely utilitarian point of view such an achievement might be counted as a gain. If those in authority were worthy of their responsibility, which would be very great indeed, economic wastes in consumption could be almost completely eliminated. This would leave more wealth to be divided among the entire group.

> "It might be argued that experts, with a view to service rather than to profits, could rationalize and standardize consumption; could define necessities, luxuries, and waste; could experiment with new values, and provide for change and improvements. Statisticians and historians could furnish for the guidance of those in authority records of the customary and habitual requirements of different classes at different times and under different conditions. Experts could work out model dietaries, design artistic houses, furniture, clothing, and ornament; the gifted could furnish a superior litera-

ture, music, and dramatic art. Corps of investigators could experiment with new foods, medicines, and sanitary arrangements. Nothing would be 'shoddy,' nothing adulterated, nothing ugly, nothing unwholesome, nothing harmful. Machinery for petitioning, for filing complaints, and for making suggestions would, undoubtedly, be part of the system. An alluring picture can be made of a great economy without 'waste.' "[1]

Not only might a well-functioning system of authoritative control eliminate or at least reduce waste; it might serve consumers better by supplying them only with those things conducive to individual and group welfare. Those in control could be expected to restrict severely the output of illth and nealth. They might see to it that everyone in the group received the basic necessities of an abundant, healthful life before anyone would be allowed to pamper his whims by smoking cigarettes, chewing gum, or jumping on a Pogo stick. In the presence of socialized compulsory care of health the patent medicine industry would disappear. In the absence of freedom of choice there would be no need for advertising. Those in control presumably would not supply injurious drugs, nor adulterated foods, nor obscene and salacious publications, movies, or plays; in the absence of freedom of choice there would be no market for bogus stock, bonds, and other "investments"; hothouses, confectioneries, soft-drink parlors, and beauty shops might be taboo; perhaps all consumers would be compelled to participate in organized sports, but commercialized recreation as it now prevails would disappear; in the absence of freedom of choice consumers would be spared from the advances of high-pressure salesmen, insurance agents, lawyers, lobbyists, and other superfluous services. It is questionable whether even authoritative control could eliminate gambling, prostitution, crime, or the consumption of alcoholic drinks. One might argue that in an economic system so well ordered, consumers would have so many other helpful outlets for their energies that the various dissipations of the present system would be quite unnecessary. On the other hand, there are some who would argue that such a consumers' world would be so dull and uninteresting that its members would be compelled to seek release and excitement in dissipation. Fortunately this question need not be answered, for although an alluring picture can be drawn of an economy dedicated to human welfare, a realist must recognize that this is merely dabbling in the world of make-believe.

Even if a system of authoritative control could be established it is questionable whether it would succeed. Human beings value freedom

[1] KYRK, Hazel, *A Theory of Consumption*, p. 39, Houghton Mifflin Company, Boston, 1923.

highly. They demand freedom to worship as they wish; they demand freedom to govern themselves; they demand freedom to think, talk, and write; and they demand freedom to consume or to refuse to consume whatever they wish. For these freedoms men have fought and will fight again. In the economic realm consumers as a group prefer freedom of choice first and economic welfare second. If the two are not entirely compatible, so that consumers must choose one or the other, there can be little doubt that consumers will choose freedom of choice. This means that to the extent that freedom of choice does not result in welfare the real problem is to find a way to economic welfare through freedom of choice. Controlled experiments with cattle, chickens, and rats have shown that some of them exercise good sense when given freedom to choose and equal access to all necessary articles of diet. Others failed to eat enough of the right things and grew up stunted and defective.[1] The task of the future is to educate consumers to make the best use of their freedom to choose.

Positive Versus Negative Freedom of Choice

An Important Distinction. Positive freedom of economic choice consists of two equally important elements: with it, a consumer has not only the right to consume anything he wishes but possesses the power or ability to exercise that right. This means that he has the requisite purchasing power to secure anything his heart may desire. Under negative freedom of economic choice one has the right to consume anything he may wish, but lacks the unhampered power of exercising that right. Theoretically every consumer has the right to own a yacht or many yachts, to drive a Rolls Royce, to fly his own airplane, to travel around the world, and to live in a palatial residence. But for most people that is a purely negative right. They also have the right to a decent plane of living which includes a sufficiency of nutritive food, a supply of good warm clothing, adequate shelter, proper health care, and a high school education. Even these minimum rights are beyond the reach of millions of consumers. It is quite idle to talk about freedom of economic choice without recognizing that under the present economic system this so-called freedom is largely negative.

Defects in Value Theory. The failure of many economists to recognize or to admit the province of negative freedom of choice has resulted in a so-called explanation of the valuation process which is incomplete and inadequate. In attempting to explain what determines the prices of commodities they have devoted scarcely a third of their explanation

[1] *New York Times*, October 1, 1939, which describes the research of Professor W. Franklin Dove of the University of Maine.

to consumer demand. The approach and by far the greatest emphasis is placed on the producer and the forces determining supply. True, it is said that both demand and supply operate like a pair of shears, and it is denied that either one alone is the more important. But whereas economists for the most part have been at great pains to explain all of the myriad forces operating back of supply they have not given equal attention to demand. On the contrary, most of them have been content merely to define demand, to distinguish between elastic and inelastic demand, and to define and discuss the law of diminishing utility. Beyond this very few have gone. A few have recognized differences in desire and differences in income as forces back of consumer demand. But why do people have different desires? And why does the utility of a commodity diminish as one consumes more of it? To answer these and numerous other questions economists would have to invade other fields of knowledge or co-operate with specialists in those fields. From the supply side economists have not hesitated to invade the fields of mathematics, physics, chemistry, and engineering in their attempt to explain the forces back of production. The time has now come when economists must join hands with psychologists, biologists, sociologists, political scientists, historians, and philosophers to formulate an accurate explanation of the forces which operate to influence consumers in their choice of economic goods and services.

Forces Restricting Freedom of Choice. As a matter of fact the theoretical assumption that consumers are free to choose what they want, and how much, is largely economic fiction. Certainly any explanation of the forces operating to determine the prices of goods which is based on the assumptions that consumers are free to choose and that in choosing they function rationally as economic men, is far removed from reality.

Among the forces operating to render negative the freedom of consumers to choose what they want, the following must be included. In the first place the national and therefore individual income is so limited that more than a majority of consumers do not have the power to acquire even the minimum decencies of life, to say nothing of freedom to choose among numerous other goods and services they might want. Another restricting force is the tendency of producers to produce that which will pay the greatest profit rather than that which will yield the greatest utility to consumers. This means that the supply of goods from which consumers must choose is restricted and may be composed largely of goods which they want only slightly or not at all. The power of habit so restricts the individual in his choosing that once he has acquired fixed consuming habits definite limits are set upon his freedom of choice. Operating in the same direction and with even greater force is the

power of custom. As a member of a group each individual is restricted in his freedom of choice by the customary consuming standards of his group. Violation of those customs will bring swift and effective punishment. Emulation is a special form of custom which widens the field of choice within a group but limits it to that group or to the one immediately above. The freedom of choice of some consumers is restricted by the desire, so far inadequately explained, to consume economic goods conspicuously for the sake of display rather than for the utility which they may yield. Certain groups of consumers are slaves to fashion in such important and extensive fields of consumption as clothing and automobiles. Through advertising in all its various forms and persuasive selling methods, producers seek with a high degree of success to turn consumer choices in directions favorable to themselves. To the extent that they succeed, consumers' freedom of choice is restricted.

A complete explanation of determinants of value and a complete explanation of why consumers choose what they do, require a careful and detailed analysis of these restrictive forces operating to influence consumer demand. This will be attempted in the following several chapters.

Summary

Freedom of economic choice is the power to choose freely among goods and services for consumer satisfaction. Authoritative control deprives consumers of this power, vesting it in some outside person or group. Formal freedom of choice is a characteristic of capitalism, but under that form of economic organization it is by no means universal. Large numbers of consumers are denied such freedom for various reasons. Wartime control of consumer choice is an outstanding illustration. Under socialism and co-operation freedom of choice would be extended, while it would be restricted under fascism and eliminated under pure communism. Although group welfare might be promoted by restricting freedom of choice, consumers value their theoretical freedom highly and will not give it up. The problem, then, is to seek group welfare while retaining free choice. This requires analysis of common but unrecognized forces restricting freedom of choice. Such forces which function continuously under capitalism include limited income, goods available, custom, emulation, desire for display, fashion, and influence of sellers through advertising and salesmanship.

QUESTIONS FOR DISCUSSION

1. In your judgment, does freedom of choice promote or retard consumer welfare? How does it affect your personal welfare?

2. To what extent are you free to choose whatever you want? Make a list of authoritarian controls which restrict your freedom.
3. Make an estimate of the number of people in the United States whose freedom of choice is restricted more than your own.
4. Have you ever been in a locality struck by some natural catastrophe? What happened to freedom of choice?
5. Would your personal freedom of choice be greater or less under a socialist economic system? Under a completely co-operative system?

PROBLEMS AND PROJECTS

1. List all restrictions on your personal freedom of choice, of which you are aware. Attempt to rate them in the order of their power over you.

2. Contrast your position as an individual consumer under the present system with what you might expect under a system of authoritative control whose purpose would be to achieve maximum consumer welfare.

3. Ask ten people at random off the campus to what extent they are free to choose economic goods and services they want. Compare results with your own responses to the above Problem 1.

5

Custom-Made Wants

Meaning and Origin of Custom

What Is Custom? First and probably most important among the forces influencing consumer demand and restricting freedom of choice is that force commonly known as custom. As a form of social control the power of custom is tremendous, yet its influence is so subtle that few consumers are conscious of it. Nystrom speaks of custom as the long-established actions, manners, usages, or practices of a group of people. In the consuming area custom is a settled disposition or tendency on the part of a group to consume according to a fixed pattern, in contrast with habit, which is a settled disposition or tendency on the part of an individual to consume according to a fixed pattern. Custom might be described as a group habit. It may be said that certain individuals have the habit of smoking, while it is customary in certain groups to smoke after dinner. In fact, an old custom, rapidly disappearing, was that which required men to withdraw to a smoking room for their after-dinner delight. Some writers assign to usages a still stronger power of control than customs. Usages in some cases are a kind of common law. For our purpose we may accept the distinction between habit and custom but include in the general term custom all that is suggested by such terms as actions, manners, practices, and usages.

In economic life customary ways of consuming are transmitted from generation to generation. This is accomplished largely through the family by means of precept, and results in an effective control of economic choice by the dead hand of ancestors. As customs become established and increasingly revered they acquire the force of law. Unless customs promote human welfare their static nature renders them effective barriers to progress.

It is reasonable to suppose that at their inception most customs had their origin in utility. Any group of individuals which initiates a food or clothing custom probably adopts that means because of its utility, but once a custom becomes established it may continue indefinitely and long after the original justification for it has disappeared. It is in such cases that custom operates as a serious restriction on freedom of consumers to choose. That sluggishness or lack of energy which we call inertia,

coupled with the influence of custom, holds consumers within well-defined limits. The gregarious tendency in man is so strong and his individualism so weak that very few consumers are able or willing to disregard group customs. In their own minds they may know that certain customs which they accept and follow are silly and useless, yet they hesitate to incur group disapproval by flouting any custom. This is really to say that most people prefer to be fools with a crowd rather than isolated sages. They dislike to be regarded as queer and can avoid that unpleasant appellation only by conforming to custom.

The power of custom is much stronger in man's consuming activities than in his activities as a producer, for the simple reason that subjective tests replace objective tests and emotions overrule reason. Competition in consumption assumes forms and leads to results radically and fundamentally different from those of competition in production. The pioneer in business is smart, but the pioneer in consumption is queer.

It should be added parenthetically that a custom is not necessarily either good or bad. At any particular time one may find in any group customs of both types. Our purpose in the following discussion is not to essay an evaluation of customs but rather to describe their prevalence and emphasize the extent to which they restrict the free economic choice of individuals.

Conditions Favoring Customs. It requires expenditure of energy to discover the existence of additional consumers' goods or new uses for goods already known. Human nature is characterized by inertia. In producing, the lure of profit is partially successful in overcoming inertia, but in consuming, the possibility of greater utility is too intangible to operate effectively. This is much the same as saying that human nature is essentially conservative. Individuals and groups are inclined to be satisfied with things as they are. There is a strong tendency to dislike change with its consequent disruption of established practices. These forces favor the establishment and maintenance of customs.

Group life is largely institutionalized. Such social institutions as the family, government, churches, and schools are essentially static. Once a group accepts monogamy or polygamy, democracy or monarchy, Christianity or Mohammedanism, compulsory free education or private schools, its consuming patterns are originally fixed and if changes occur they usually come slowly. Group institutions thus favor the establishment and continuance of custom.

Stratification of groups into classes is universal. Regardless of the basis of stratification, the favored ones at the top enjoy a more abundant economic life than those in the lower strata. Their favored position carries with it not only the power more fully to satisfy their wants, but also

power to maintain the *status quo.* Change is resisted through fear that any innovation may weaken their position or even displace them. These small but powerful groups have a definite place in the establishment and maintenance of customs which accept the existing order. Numerous illustrations are available, but one of the most striking is the tenacity with which military and naval officials and munitions makers cling to the belief that war is inevitable as the only means of settling serious international disputes. To accept any other view would weaken their economic position which they regard so highly. This is not to impugn their standards of patriotism but to suggest that their economic status is a powerful determining influence.

Isolation is a force favoring custom. Whether the isolation results from physical, political, racial, or linguistic barriers, the results are identical. By these means groups are cut off from others, and the transmission of ideas from one group to another is either hampered or prevented. Within the limits of its own borders each group develops characteristic products and methods of consuming which frequently could be adopted to advantage by other groups. If a free interchange of group experience were possible, new methods would constantly challenge accepted customs, but such is not the case. While modern transportation has done much to break down physical barriers, there are still many groups whose contacts with others are limited. It is a curious anomaly that in those parts of the world where transportation has reached its highest development possible beneficial effects have been largely offset by a growing tendency toward nationalism. The breakdown of a physical barrier seems to be the signal for the erection of an artificial political barrier. Racial distinctions are as old as the world. When racial differences assume the force of prejudice, members of any group are all too effectively cut off from other groups. In those parts of the world in which groups live in close proximity yet speak different languages, their inability to converse freely operates as an effective barrier to interchange of ideas. "Little Germanies" and "Little Italies" in large American cities effectively illustrate the power of linguistic isolation.

Private home life is, within a group, a special form of isolation which fosters and maintains custom. Like the clans which preceded it, the family is a closely knit consuming unit whose consuming practices have a strong tendency to assume the force of custom. Established ideas of what should be consumed, and how, are passed down from generation to generation, acquiring additional prestige with each transmission. Each generation acquires new habits which, passed on to children, assume the force of custom. So completely are these established usages

adopted that anything new from outside must overcome a natural inhibition to its use. New foods may be discovered, as well as new ways of preparing them, but the family is likely to continue to consume potatoes prepared as mother or grandmother used to cook them.

Illiteracy constitutes another special kind of isolation which renders individuals and the group less susceptible to the adoption of new ideas. Illiteracy as used here is confined to its narrower meaning of inability to read or write. In a broader sense ignorance is probably one of the strongest allies of custom. If that is true it seems equally true that illiteracy is the main support of ignorance. Inability to read or write narrows the experience of groups to that obtained from actual contact with near-by neighbors. The only way a new idea can be caught is by word of mouth. If infrequency of travel also characterizes the group, as is usually the case, there is little opportunity to break the power of custom.

Conditions Opposing Customs. In a general way it may be said that any forces operating to break down the conditions discussed above are in opposition to customs and their continuance. Specifically and most significant are education, travel, and freedom of thought, of speech, and of the press. When education becomes institutionalized in the school it frequently operates as an ally of custom. This is perhaps most likely in primary and secondary education, with the tendency somewhat less strong in colleges and universities. But stereotyped though the curriculum may be, the very educational process is in opposition to such isolation from new ideas as that brought on by illiteracy. Travel as a special form of education is a means of breaking down physical and political barriers. Freedom of thought, of speech, and of the press are powerful allies of progress and opponents of a *status quo* unsatisfactory to a majority of the group. Regardless of the relative merits of advertising, there can be no doubt that as a special form of education it has succeeded in breaking down certain customs. For example, the crumbling of the customary taboo against smoking among women has been due in no small part to the influence of advertisers.

Research into the unknown is an effective means of shattering custom. Pioneers on the fringe of human knowledge are continually discovering new goods and new methods capable of expanding human welfare. Among the first things which research workers cast out completely are rule-of-thumb methods and customary practices. The possibilities of a super race have been envisaged by nutrition experts, and achievement waits only for the power of research and knowledge required to break down customary food habits. For example, research at the city's infirmary in St. Louis indicates that the span of active life may be increased by utilizing certain minerals and organic substances. Proper diet and eating

habits have shown in 271 cases that degenerative diseases can be combated successfully.[1]

War is a powerful opponent of custom. There are those indeed who would justify war as a stimulus to progress. One need not subscribe to such an extreme view to recognize the truth that when a nation is engaged in what it regards as a struggle for its existence urgent necessity sweeps aside useless wasteful customs. It does not follow that customs so displaced are replaced by others which contribute more to human welfare, but the presumption is strongly in that direction.

The acquisitive instinct of man as a producer breaks out in that form of rivalry for consumer favor which we call competition, and so operates as constantly to challenge custom. In their quest for profits producers persistently seek new goods and new uses for old goods as a means of currying consumer favor. As a result such customs as artificial lighting with oil lamps, preserving foods in cellars or iceboxes, and traveling on steam-propelled trains give way, more and more extensively, to the newer customs of electric lighting, gas or electric refrigeration, and transportation by automobile or airplane.

Customary Consumption of Food

Food Customs of National Groups. Although desire for food is one of the most powerful inborn tendencies, consumers are restricted in their choice not only by individual tastes and available foods, but also by custom. Regardless of the locality in which one lives there are at least twenty elements which are essential for normal growth and development. These include ten minerals, six vitamins, water, and the three energy-yielding food constituents fat, protein, and carbohydrates. Of the ten minerals required only calcium, phosphorus, iron, and iodine are likely to be deficient.[2]

The extent to which group diets are sufficient or deficient in these elements is in large degree dependent upon food customs. A study of 105 family diets revealed 61 per cent receiving less than 3,000 calories per man per day. Italian consumers received the most, half of them securing the required standard. On the other hand only 30 per cent of the Jews and 19 per cent of the Negroes were receiving standard amounts. While Negroes had a greater quantity of food and spent more for it they received the least nourishment. In all cases mineral elements showed a high percentage of deficiency. There were some Jewish homes in which

[1] *New York Times*, July 18, 1943, which describes the research carried on by Dr. William D. Kountz and Dr. John G. Steinle.

[2] Hawley, Edith, *A Short Method of Calculating Energy in Diet*, Technical Bulletin, No. 105, United States Government Printing Office, Washington, 1929.

no milk was consumed, yet Roman cheese costing $1.25 a pound was bought in small quantities! As a result most of the children in those families had rickets.[1]

The influence of religious customs on diet is especially great among the Jews. They have carefully prepared lists of many foods whose consumption is absolutely forbidden, and others which are forbidden at certain times. By restrictions on the use of meat there has been developed a fondness for fish which is beneficial. Restrictions on the use of butter and meat together have reduced the consumption of vegetables, which is detrimental. The average Jewish diet "is inadequately balanced, over-rich, and over-seasoned."[2]

In the words of Professor Patten, "Each nation has a strong tendency to love what its environment can furnish with the least expense." But since Professor Patten was one of those economists who believed in the assumption of the economic man, the "strong tendency" which he observed must be discounted. There can be no doubt that in food customs the tendency operates more forcefully than in the consumption of other commodities, yet in the consumption of food the power of custom is so great that many available commodities are not used. Certain foods which are considered delicacies by one group are positively repulsive to another; yet in many cases they are available to both. Americans customarily eat corn, but Englishmen and Frenchmen regard it as chicken feed and abhor its consumption by humans. In Japan seaweed and candied grasshoppers are eaten. Although these delicacies are available in other lands, custom condemns their use. The approved diet of North American Indians included snakes and lizards, while that of contemporary Frenchmen favors snails and frogs' legs. Flesh of small species of octopus is a Neapolitan delicacy, while eggs of the Volga sturgeon, commonly known as caviar, are held in high favor by Russians. Pickled pigs' feet are popular in Germany, and moldy cheese with skippers delights Englishmen. Fried rhinoceros hide is an African treat which few other groups can enjoy. In China not only powdered deer horns, but the flesh of rats, cats, dogs, and mice is consumed.[3] Some tribes in New Guinea find human flesh a pleasant kind of nourishment.

A typical Eskimo breakfast consists of strong tea, frozen raw fish or meat, and dried fish with blubber dipped in oil. If guests are present such a delicacy as raw putrid liver or walrus intestines would be added. An especially rare treat available only to Eskimo hunters is a special kind of

[1] Phillips, Velma, and Howell, Laura, "Racial and Other Differences in Dietary Customs," in *Journal of Home Economics*, vol. 12, pp. 396–411. [2] Schapiro, Mary L., "Jewish Dietary Problems," in *Journal of Home Economics*, vol. 11, p. 53.

[3] Fairchild, David, "The Palate of Civilized Man and Its Influence on Agriculture," in *Journal of the Franklin Institute*, vol. 185, No. 3, p. 308.

clam chowder. Within thirty minutes after the death of a walrus, the hunters begin eating it, starting with the warm clam chowder taken from its stomach.[1]

Other less striking and less repulsive practices are observable among national groups. Fish, flesh, and blubber are associated with Eskimos, while rice suggests the Chinese diet. Baklava, a dessert resembling shredded wheat covered with honey and nuts, and helva, a delicious confection, please the palates of Turks. While Germans drink beer, Frenchmen prefer smooth wines, and some Americans demand hard liquor.

Food Customs of Localized Groups. Any impression that all members of a national group consume the same foods must be corrected. While it may be true that there is a tendency for food customs to be universal in small countries, the tendency is much less strong in larger nations. In the United States large quantities of sea food are consumed by those living on or near the coast, while few residents of the Middle West have acquired a taste for such food, although modern refrigeration and transportation make it available. Boston housewives insist that brown-shelled eggs are superior, while women of New York insist upon those with white shells. Boston brown bread is scarcely known by white-bread consumers of the Middle West or corn-bread devotees of the South. New Englanders eat pie for breakfast, Middle Westerners prefer it at their noon meal, while city dwellers of Middle Atlantic states consume it only with their evening meal, which is called dinner. Buckwheat cakes and sirup are preferred by some groups to the chicken and muffins which delight others.

Food Customs Are Acquired. Further illustrations are unnecessary to emphasize the fact that environment and the group into which one is born are important determinants of food-consuming customs. The accident of being born in China, Turkey, or the United States is an important factor in determining consumer choice of food. Likewise the accident of being born in one section of the United States rather than another determines through the lifetime of the consumer the kinds of food he will consume. The religion into which one is born will influence his diet. All this is to say that there is very little rationality in the choosing of food. It also suggests that although desire for food is an inborn tendency the types of food demanded by consumers are the result of acquired habits.

Individual Differences in Food Tastes

There are, however, certain individual differences in taste which have not been explained. Some people are extremely fond of liver, brains,

[1] Cremeans, Lola M., "Food Habits of the Eskimo People," in *Journal of Home Economics*, vol. 22, pp. 263–269.

tongue, and grapefruit, while to others in the same group these foods are positively repulsive. Some economists have recognized differences in desire as a significant force back of demand, but the co-operation of biologists and psychologists is needed to explain the reasons for these differences. The gustatory sense alone is insufficient to explain them. While the actual taste of chocolate or cherries, for example, is unpleasant to some people, the decision not to consume some other products is frequently determined by appearance or smell. The very sight of calves' brains, eel, or lobster is sufficient to turn many potential consumers against them. Without even tasting these foods which please so many people, others refuse to include them in their diet.

The olfactory sense is an equally critical guide. The odor of frying potatoes, of steaming coffee, or of boiling cabbage is sufficient to attract or repel possible users. If the odor of Limburger cheese is repulsive to a person, he will make no effort to discover its effect upon his sense of taste. Apparently the physical and nervous systems rebel. The extent to which olfactory senses vary is revealed by a test made by Dr. Albert F. Blakeslee of the Carnegie Institution's Department of Genetics, experimenting at an international flower show in New York. Thousands of men and women disagreed on the relative pleasantness of odor of two vases of flowers, one containing freesias and the other leucocoryne, popularly known as the "Glory of the Sun." Among the nearly 7,000 women who expressed their judgment on freesias 17 per cent could detect no odor at all; and of those who did, 53 per cent said it was weak, 29 per cent found it medium, and 18 per cent classed it as strong. Of the same group 75 per cent found the odor pleasant, 15 per cent regarded it as indifferent, and 10 per cent classed it as unpleasant. Among men smelling the same flowers 19 per cent detected no odor; and of those who did, 57 per cent said the odor was weak, 27 per cent called it medium, and 16 per cent said it was strong. On the test of pleasantness 68 per cent of the men found the odor pleasant, 21 per cent called it indifferent, and 11 per cent said it was positively unpleasant. Reporting on the leucocoryne flowers, 32 per cent of the women and 24 per cent of the men found the odor distinctly unpleasant, while 57 per cent of the women and 65 per cent of the men regarded the odor as pleasing.[1]

These results are interesting and informative. They indicate that a large number of men and women would never buy certain flowers. Carried over into the realm of food, similar results would no doubt follow. But while these tests reveal differences in the sense of smell we do not yet have an explanation as to why all things do not smell alike to all people.

[1] "Demonstration of Differences between People in the Sense of Smell," in *The Scientific Monthly*, vol. 41, pp. 72–84.

It is interesting to observe that when a child under authoritative control of his parents is compelled to eat certain foods regardless of his own wishes in the matter it may happen frequently that he acquires a fondness for them. Such compulsion is just as likely to work in the opposite direction and to reinforce the original inhibition so strongly as to turn him forever against those foods. In the case of adults similar tendencies are observed. To those who can subject their senses of sight and smell temporarily to experiment with new foods the way is open to previously unrealized gustatory delights. This is simply saying that to the extent rationality replaces custom and habit the area of freedom of choice is widened. Thus the more an individual has traveled about the world, the larger the list of foods with which he is familiar and the pleasures of which he has enjoyed. By the same token the provincial consumer has closed to him forever the satisfactions which might be realized by many kinds of food outside the pale of his limited diet.

World War II swept many consumer customs into discard, some of them temporarily, some of them permanently. Dietitians for the Civilian Conservation Corps found it impossible to satisfy the tastes of young men from all sections of the country. Boys from New Mexico and Texas wanted their customary chili and beans; those from New York City wanted spaghetti and meat balls; Louisianans wanted cane sirup, but of course Vermonters would not eat sorghum. Finding that boys from all sections liked beef, chicken, milk, ice cream, and fresh fruits, the dietitians attempted to give them enough of what they wanted plus enough more of what they should have to keep them healthy.[1] Army dietitians encountered the same problems in preparing diets for the rapidly growing Army of the United States in 1942. They reported that Southern boys wanted their hominy and grits, while the Eastern soldiers wanted their sea foods. Like the Civilian Conservation Corps dietitians, the Army dietitians catered to the local whims of the men to a certain degree, but their chief purpose was to furnish an adequate, well-balanced diet. It was the opinion of the Army food consultants that the men would develop a cosmopolitan appetite which would affect the food habits of the nation for generations to come.[2]

Still another factor determining individual choices of food is the susceptibility of some people to poisoning by certain products. Many consumers have what is called an allergy for one or more foods. Eggs frequently affect people in this manner, while such a wholesome food as milk is also an allergy to some people. It is easy to see how this phenomenon can be the starting point for a food custom in a poorly in-

[1] STINNETT, Jack, "Washington Day Book," in *Newark Advocate,* April 26, 1941.
[2] BARBER, Mary I., in *New York Times,* October 20, 1942.

formed localized group. If one or two members of the group suffer food poisoning, and practically any food may be an allergy to someone, the offending product might be removed forever from the group's approved list of commodities. Perhaps many food customs had their origin in this way.

Food-consuming customs do change. Comparing the annual average per capita consumption of certain kinds of food in the United States in the period 1909–1916 with that in the period 1937–1941, an investigator found a decline in the consumption of meat, poultry, fish, potatoes, and wheat flour. On the other hand, consumption of fluid milk and cream, evaporated milk, cheese, ice cream, eggs, beans, citrus fruits, canned fruit, canned vegetables, sugar and sirup, butter, coffee, tea, chocolate, and spices increased, in some cases very considerably.[1]

Changing food customs are not necessarily desirable, however, as revealed by a study of the food habits of eighty college students. It might be presumed that college students should know the types of food they ought to eat for good nutrition. The following results indicate either lack of information or a misuse of the freedom of choice. A two-day record of food consumption which the investigator thinks represents the individual food habits of these eighty students shows that 23 per cent had no milk; 34 per cent no green leafy vegetable; 22 per cent no citrus fruit; 10 per cent no fruit of any kind. It was revealed further than 20 per cent had no whole-grain cereal. On the other hand, whereas only 2 per cent had no meat, 37 per cent had three or more servings of meat each day. Almost all of the group—96 per cent—ate between meals. Between-meal items consisted chiefly of candy, cake, ice cream, cookies, sandwiches, Coca-Colas, and fruit, in the order named. The average member of that group spent 13 cents a day on between-meal eating. Nearly a third had no breakfast or an inadequate breakfast, a sixth had inadequate lunches, and 13 per cent had inadequate dinners.[2]

A much more extensive survey of college students disclosed that 71 per cent had seven or more servings of milk a week. Those having green and yellow vegetables were 60 per cent; those having citrus fruits 43 per cent; and those having whole-grain cereals 34 per cent. Like their fellow college students the members of this group liked meat, 86 per cent of them having seven or more servings a week.[3]

A National Conference on Nutrition for Defense was held in Wash-

[1] WELLS, O. V., "America's Changing Food Consumption, 1909–1941," in *Journal of Home Economics*, vol. 34, pp. 436–467.

[2] SHAW, Mary Margaret, "A Study of the Food Habits of Eighty College Students," in *Journal of Home Economics*, vol. 32, pp. 614–615.

[3] REYNOLDS, May F., and others, "The Dietary Habits of College Students," in *Journal of Home Economics*, vol. 34, pp. 379–384.

ington in May, 1941. The advent of a war economy suddenly brought into sharp relief the relationship between nutrition and health. Just prior to the convening of the Conference, the Committee on Food and Nutrition of the National Research Council published nutritional standards, recommending the minimum daily allowances of riboflavin, iron, thiamin, vitamins A, B, D, calcium, protein, and nicotinic acids. It was made clear in the Conference that American food-consuming practices fell far short of these minimum standards. The Bureau of Human Nutrition and Home Economics of the Department of Agriculture estimated that three fourths of the people of the United States did not then have what could be considered a good diet and that at least forty million people were suffering from a very bad diet. The findings of the Conference showed clearly that an improved diet would diminish such deficiency diseases as pellagra, rickets, and scurvy. It was estimated that if all consumers had a desirable nutritive diet it would be necessary to double the production of vegetables and fruits. We should have to have 70 per cent more tomatoes and 70 per cent more citrus fruits; 35 per cent more eggs; 15 per cent more butter; and 20 per cent more milk. One of the reasons for the food shortage in 1943 was doubtless the fact that for the first time in their lives some millions of men were being fed a diet which contained foods of this type.[1]

Clothing Customs

Why Do We Wear Clothing? Unlike the desire for food, consumer demand for clothing does not result from an inborn tendency. While most people in the world wear some clothing there are those who wear none at all. Any attempt to explain the use of clothing on the basis of physical need alone would be futile.

Decisions as to whether to wear any clothing at all, and if so how much and what kinds, are made largely by the group rather than by individuals. In other words, custom lies back of consumer choice for clothing. But what lies back of the custom? Why do people wear any clothing? Why do costumes vary so strikingly among groups? If utility alone were the guide the presumption would be justified that in a particular climatic zone certain articles of dress would possess greatest utility, leading to their universal use. But such is not the case.

When we turn to anthropologists, sociologists, and psychologists for an answer to the first question several explanations are found. The lack of unanimity is confusing. Sumner accepts the view "that things were

[1] There are many periodical sources of information on the National Conference on Nutrition for Defense. A good summary will be found in Wilson, Stephen, *Food and Drug Regulations*, American Council on Public Affairs, Washington, D. C., 1942. See also the references on page 41 of this volume.

first hung on the bodies as amulets or trophies, that is, for superstition or vanity, and that the body was painted or tattooed for superstition or in play. The notion of ornament followed."[1] Savages lying in ashes, dust, sand, or mud for warmth or coolness discovered that protective layers guarded them from heat, cold, and insects. The original utility of certain attachments to the body was thus discovered and expanded. Prevalence of superstition led to very careful copying by other members of the group, thus developing group costumes. Any variations from these clothing customs involved fearful consequences which few had the courage to risk.[1]

Others explain the origin of clothing as the result of man's imitativeness. In those countries inhabited by fur-bearing animals it is held that man was quick to see the warmth and protection to be yielded by animal skins. In skinning trophies of the hunt preparatory to eating, primitive man may have experimented by placing himself inside the animal covering. Finding it satisfactory, others imitated the practice and a custom based on original utility was established.

The fact that clothing is not universally worn for the sake of modesty is demonstrated by its total absence among some people. Experiments and observation of results following the introduction of clothing among such groups seem to justify the conclusion that clothing is not a result of shame, but rather a cause. Among Christian women modesty requires covering the greater part of the body except the face; among most Moslem women the one part of the body which must be covered is the face.

Accepting the suggestion that clothing was originally adopted for protection from climate and insects, Miss Bliss is still not satisfied. She advances the suggestion that of all animals man is the most completely naked. He has no covering of hair, fur, feathers, or scales. This complete lack of a protective covering has led him to supplement nature.[2]

A modern psychologist declares that neither warmth nor modesty is a very important consideration in the choosing of clothing by most people. The well-dressed person of today, psychologically speaking, wears clothing which yields security and brings recognition, response, and new experiences. Security is described as the feeling attendant upon wearing clothes chosen for suitability to the wearer and the occasion. Recognition is the approval which one's clothing wins from friends and associates. Response is the effect of clothing upon other people. Color, style, and the poise with which clothing is worn all make their impression. The fourth

[1] Sumner, William Graham, *Folkways*, p. 429, Ginn and Company, Boston, 1907.

[2] Bliss, Sylvia H., "The Significance of Clothes," in *American Journal of Psychology*, vol. 27, pp. 217–226.

function of clothing, according to this view, is to satisfy the universal hunger for new experiences. By changing and experimenting with clothing individuals may secure a peculiar thrill of satisfaction and a sense of adventure.[1]

From these various explanations of the origin of wearing clothes, the general conclusion may be drawn that in the past, in some cases, clothing was adopted as a means of protection. Its continued use is to be explained in large part by its ability to protect the wearer. There can be no doubt that consumers choose their clothing to a large extent with regard to their peculiar occupational needs. But to recognize the influence of this factor in choosing clothing is not to deny the presence of other forces equally powerful although perhaps less necessary. The influence of individual and group concepts of beauty, as reflected in harmony, color, and lines, is probably no less important a reason why clothing is worn. These decorative functions of clothing will be discussed in a subsequent chapter dealing with fashion.

Variations in National Costume. An interesting feature of the custom of wearing clothing is the development of a national dress. In his treatment of the psychology of dress, Parsons describes the changes which have taken place from the Middle Ages down to 1920. The four main underlying influences which he finds operating to affect national costume are religion, royalty, fashion, and war.[2] The formal and distinctive dress of Turkish people illustrated, until recently, the religious influence. The brimless fez was worn to enable a devout Moslem to remain covered in the mosque and yet permit touching the forehead to the floor while praying. Full-seated trousers were designed to permit the wearer to sit with legs crossed, while the peculiar slipper-like shoe could be easily removed upon entering the mosque. The influence of royalty has been more pronounced in the past than it is at present. Under the leadership of Edward III, Englishmen discarded long hampering robes for what was regarded as the more satisfactory dress of that period. The influence of royalty may be seen operating negatively through the former numerous sumptuary laws regulating the type of dress for different classes.[3]

The influence of war is especially apparent in changing the costumes of fighting forces. Serviceability, comfort, and power to conceal have become increasingly important features in clothing soldiers. The influence of a long war and of changes in military uniform are often reflected in civilian costume. The effect of fashion is so significant that the entire

[1] BANE, Lita, in *New York Times*, July 17, 1935. [2] PARSONS, Frank Alvah, *The Psychology of Dress*, Doubleday, Doran and Company, New York, 1920.

[3] BALDWIN, Frances Elizabeth, *Sumptuary Legislation and Personal Regulation in England*, Johns Hopkins University Studies, vol. 44, Baltimore, 1926.

Chapter 8 is devoted to it. The decorative function of dress will be included in the treatment of fashion.

After World War I there was a significant trend toward the adoption, by peoples all over the world, of what is commonly called Western or American dress. The distinctive and colorful costumes of China, Japan, Turkey, Greece, Bulgaria, Italy, and Holland seem to be disappearing in everyday usage. This is difficult to understand, for probably in no case is the new costume superior to the one displaced in its ability to protect and decorate the wearer. The explanation may be found in the wish of those people to emulate the dress of some nation which had achieved remarkable economic progress. Perhaps the feeling prevailed in many countries, as it did in Turkey under the influence of its leaders, that the old costume was a mark of inferiority which set off the wearer as a member of an economically backward group. Strong pressure was used to break down the influence of religion and custom in national dress. The same forces which operate on an individual to secure conformity to group practice were apparently at work on some of the smaller groups to secure conformity to the practices of larger and more economically powerful groups. Deliberate emulation of one group by another is something new. In all these cases the power of the group operating through custom is influential in determining individual choice of clothing.

Ceremonial and Sports Clothing. The academic gown, judges' robes, and vestments of the clergy are special types of clothing which are of no special usefulness in protecting the wearer. There is no vestige of original utility in such differences of garb. Their purpose is so entirely that of setting the wearer off as the member of an enviable group that further discussion will be deferred to Chapter 7, on conspicuous consumption.

The influence of sports on clothing is a comparatively modern development. What one shall put on or take off to participate in a particular sport is a matter of serious concern upon which the group speaks with authority. When boys go fishing they simply get a pole, line, hook, and some worms and usually bring home the fish. From their elders, however, custom demands that they first visit a sporting goods or hardware store to secure a complete and approved outfit. From elaborate reel to wading boots no detail is overlooked, nor is any opportunity lost by alert businessmen to impress upon fishermen the absolute need for every item.

When country boys want to ride a horse they simply emulate their ancestors by springing lightly to the bare back of the animal, but to the urban dweller that is not riding. To be a proper horseman or horsewoman the city rider must have a complete riding habit made of the best of materials, supplemented with genuine leather boots and an elaborate saddle.

Customary bathing costumes have passed through interesting cycles. It is a far cry from the gay '90's when men and women entered the water almost entirely covered, to the beach costume of 1944 obviously designed to expose the maximum legal limit of nakedness both to the sun and to admiring eyes.

So far has the influence of custom gone that so simple a recreation as walking now requires correct costume. Whether at the seashore, in the mountains, or on the ranch, whether playing ball, tennis, or hockey, whether skiing, sailing, or hunting, the group requires that in all cases the individual participant must be clothed in the approved manner. The costume may be ugly, stupid, useless, or expensive, but it requires a courageous individual to flout group authority by refusing to wear the customary garb. As a result the area of individual freedom of choice is tremendously restricted. Millions of dollars are spent on clothing not because purchasers have an original desire for it, but because the group demands conformity.

Vestiges of Former Customs. A critical examination of customary clothing reveals numerous vestiges of former customs which have almost or entirely lost their original significance. Why do men wear trousers and women skirts? Why do men crop their hair while women wear it long or at most merely bob it? Why do men wear collars and ties, while women expose the neck? Why do men wear heavy felt hats and caps, while women wear fragile head dress? Why does either sex wear any head dress at all? Why do men encase their bodies in heavy, tight-fitting vests? For what reason do they top this off with a still heavier coat? Why do their coats have lapels, and buttons on the sleeves? Why do men's coats button on the right, while those of women button on the left? Why do the trousers of men's business suits have cuffs, while it is considered improper to have cuffs on the trousers of formal morning or evening clothes?

In all these cases and many others like them explanations may be found if one traces the development of group costumes far enough back. In few cases, however, will any justification be found for these customs. It is said that men wear trousers to allow greater freedom of movement, while women wear skirts the better to hold children on their laps. No plausible explanation has been discovered for the differences in length of hair. Some attempts have been made to explain the shortness of masculine hair as a means of defense in military conflict. It is contended that in primitive times a long beard and flowing hair served as too convenient a means of a victim being held preparatory to receiving the death blow. The differences in custom cannot be explained on the basis of comfort or convenience, for if the custom of short hair had such a basis it would prevail among women also.

One can trace the development of styles in neck dress through a long period of time without finding an adequate answer to the question why modern men wear high-neck clothing. There is no apparent reason or utility; it is simply the custom. Much the same may be said for the deep-seated custom of wearing hats. In tropical climates the hat serves as a protector from the sun, while in frigid zones some form of head dress is necessary as protection against extreme cold. But the wearing of hats in temperate zones is difficult to explain or justify on any basis of utility. Again it is simply the custom. Indeed it is such a powerful custom that most men feel incompletely dressed if they appear on the street without a hat, while the chagrin of a hatless woman at an indoor function is pathetic.

The customary three-piece suit which modern men wear retains distinct vestiges of former military costume. The vest is explained as a carry-over from the former metal jacket worn as a protection against enemy spear thrusts. The heavy outer coat is the modern counterpart of the military blouse with its numerous useful pockets and tight buttoning of the front. When that type of blouse was common, men found it more comfortable upon entering a warm climate or building to open the garment at the neck, turning down the corners. The modern customary notched lapel with a buttonhole on the left lapel is a vestige of that ancient practice. Although the modern gentleman never thinks of turning up his coat so as to fit snugly around the neck, that is the only possible reason, aside from custom, for the cut of men's coat collars. Indeed, so far removed is the custom from its origin that in many suits the buttonhole itself is simulated rather than real, while the necessary button on the right side of the collar has long since disappeared. In the days when men were swashbuckling fighters there was a real purpose behind a right coat sleeve slit to the elbow. In case of sudden necessity the wearer could quickly bare his sword arm to the elbow. When the struggle was over the sleeve was then replaced and buttoned down to the wrist. The modern inch-long slit with two or three buttons on each coat sleeve is the meaningless vestige of this former practice.

In the days when men were primarily warriors and women combined child care with productive work, another common custom was originated. Whether man's weapon was a sword or gun he was in most cases more skillful in the use of his right hand. In order to keep that hand free for defense or attack, buttons and buttonholes on his coats were so arranged that he could manipulate them with his left hand. Since most women also were more skillful with their right hands it was customary to carry a baby on the left arm so as to have the right arm free for work. This led to the custom which is still retained of arranging the buttons and button-

holes on women's coats so that they can be manipulated with the right hand.

When travel by horseback was the most common means of transportation the customary method of wearing trousers was that of a loop under the instep fastened to the trouser leg to hold it down. As travel by horseback gave way to other means of transportation customarily long trousers grew cumbersome and inconvenient, and the practice of turning them up supposedly marks the beginning of the modern custom. If there is any plausible reason why trousers of morning and evening clothes do not have cuffs it is to show that the modern wearer, like his horseman ancestor, is a gentleman freed from necessity of physical labor. The customary stripe down the side of evening trousers is a carry-over from the days when men wore tight-fitting trousers which buttoned down the side. The stripe at first was in the nature of a flap to conceal the buttons. The swallow-tail coat of the evening suit is the meaningless result of an evolution in the knee-length coat. Former wearers of such garments found it necessary for comfort to slit the back and turn back the lower front corners when riding horseback. Since the riding of a horse was associated with men of means the gradual change in cut of the coat led to the modern evening coat.[1]

These illustrations of the origin of clothing customs have been chosen practically at random. Others equally interesting could be chosen so as to extend the discussion indefinitely. The purpose of this chapter, however, is not to trace the origin of customs but to emphasize the power which custom plays in determining the economic choices of individuals. Enough has been said to demonstrate clearly the extent to which freedom of choice in selecting clothing is restricted by customary dictates of the group.

Summary

Custom is a long-established group practice or usage. It is strongest in the consuming aspects of economic life, frequently having the force of law. Among conditions fostering custom are inertia, social institutions, social stratification, isolation, home life, and illiteracy. Education, research, war, and competition operate to break down customary consumption. Although desire for food is inborn, satisfaction of that desire is severely restricted by the group into which one is born. Explanation of individual differences in taste requires the aid of biologists and psychologists. Desire for clothing is acquired and consequently still more influenced by group custom. The decorative function of dress is probably more influential in determining choice than the protective. Modern

[1] Wolff, Edwin, *Why We Do It*, The Macaulay Company, New York, 1929.

clothing customs reveal many meaningless vestiges of former customs, some of which had their origin in utility, while others never possessed any apparent usefulness.

QUESTIONS FOR DISCUSSION

1. Is it "reasonable to suppose that at their inception most customs had their origin in utility"? Name several customs and suggest their utilitarian origin.
2. Can you suggest any conditions favoring custom, in addition to those named in the text?
3. Do you agree that education, research, competition, and war tend to break down customs?
4. Compare the range of your usual food choices with that of an individual in another section of the United States or in another country. To what extent are the differences based on custom?
5. Why do you wear clothing? Why do you wear the particular clothing you now have on?
6. What type of clothing would you wear if you had been born in Haiti? Cuba? Bavaria? Tirol? Alaska? China?
7. Give several illustrations of the influence of religion on food and clothing customs.
8. Does the influence of custom on consumer demand harmonize with the traditional concept of an economic man?

PROBLEMS AND PROJECTS

1. Draw up a list of ten distinctive local customs; evaluate their effect on freedom of choice and consumer welfare.

2. Write a paper on current influences tending to weaken certain customs. Why, for instance, is smoking becoming more prevalent among women?

3. Compare and contrast distinctive customs in your vicinity with those prevailing in another part of the United States or in another country with which you are familiar.

4. Make a list of foods you do not like and analyze the reasons for your distastes.

5. Contrast the clothing customs of men and women and seek to discover their origin. Evaluate their comparative contributions to consumer welfare.

6. Write an essay, based on your own observation, on the influence of sports on clothing.

6

More Custom-Made Wants

Customs and Emotions

Religious Customs. The deep-seated power of custom is most evident in those sectors of life which are closely related to human emotions. From the beginning of life to its end customary practices prevail. Outstanding are those customs associated with birth, marriage, and death. Significant throughout the span of life is the influence of religion, which by its very nature builds on custom. The power of ancestors is shown in determining what shall be worshiped, and how. In all religions, from the worship of natural forces by primitive people to the worship of Deity by modern men, the influence of custom is evident. From the extensive ceremonials surrounding the Catholic faith to the simplicity of the Quakers, the difference in the power of custom is largely a matter of degree.

In all religions the influence of bans is as significant as the power of positive admonitions. The great influence of religion on economic choice is seen in authoritative decrees as to what people shall or shall not wear, as to what they may or may not eat, as to how they may or may not act. Those most strongly influenced by religious regulations are officials of the church. In the most rigidly regulated faiths the very vestments which they must wear set them apart from others in the group. Restrictions on their mode of living and regulations governing their conduct of religious services reflect the power of custom and limit their freedom of choice.

The church edifice itself shows the influence of custom on architecture. From traditional stained-glass windows to symbolical spires pointing toward heaven this influence is seen. In contrast to the comfortable seats in a modern theater the traditionally uncomfortable pews in a church reflect the influence of former generations of Puritans. In Catholic and certain Protestant churches custom requires the kneeling bench. This is a concession to cleanliness and comfort, while plush-covered altars carry this tendency to what some regard as an extreme. The extent and elaborateness of pulpits, altars, vestries, and choir lofts vary among different churches. The religious service itself is entirely customary. Ritualistic ceremonies differ largely in degree. Even so simple a service as that of the Quakers is based upon a customary method of worship.

While Protestant denominations are less given to ritualism than other faiths, there are those who believe that the tendency is toward more rather than less ceremony. Thus Mr. Webber quotes a dealer in religious goods:

> "An astonishing thing is taking place right here in my store. . . . A few years ago I used to sell candles, incense, and embroidered chasubles to Roman Catholic priests. Their people would drop in and buy a prayer book or a rosary. Protestants would pause briefly before my window, glance at it disapprovingly, and then walk away. But what a change today! That gentleman with the clerical collar and black rabat who just left the store is a Lutheran. He bought a whole carton of pure beeswax candles, a pound of Jerusalem incense, and there is a richly embroidered green cope in the glass case upstairs that always catches his eye. Episcopalians not only buy beautiful prayer books, but lately they are buying rosaries and even plaster images of the Blessed Virgin. A Methodist parson also dressed in clericals, came in last week and bought a brass cross for his altar. Two of the most recent Methodist churches in this city have real altars with crosses on them. I sold a pair of seven-branched floor candlesticks to a Presbyterian church a month ago, and a processional crucifix, and a censer to a Lutheran parish. Nowadays when a man in clericals comes in, he may be a Roman Catholic priest, or an Episcopalian, or a Lutheran, or even a Methodist or a Presbyterian."[1]

The influence of religious custom on economic choice is by no means confined to church officials. The 56,000,000 members of churches of all denominations in the United States require millions of dollars' worth of economic goods prescribed by their regulations. Many of these members are also definitely removed from the market for certain specified goods by restrictions of their faith. It has already been shown how Jews must eat certain foods and refrain from others. Similar restrictions regulate Mohammedans and Catholics. Mohammedans also continue the custom of washing their feet and removing their shoes before entering their mosques. This leads to the practice of wearing slipperlike shoes which are easily removed and replaced and in turn accounts for a prevalence of flat feet. The first thing a Mohammedan does to a pair of Western-style shoes is to cut out the counter or bend it over. While Mohammedans must never eat ham, Catholics need abstain from meat only on Fridays, when fish is often eaten instead. The very large demand of Catholic countries for fish is said to have led to the discovery of the rich New-

[1] Webber, F. R., "Are Lutherans Going Ritualistic?" in *The Christian Century*, June 26, 1935, p. 852.

foundland fishing banks soon after the first voyage of Columbus to America. Catholics also require holy water, incense, and beeswax candles. Among Protestant denominations, Baptists require a built-in baptistery in the church. Customary observance of the Lord's Supper requires specially made individual glasses for serving grape juice, which has replaced the original wine. Modern standards of hygiene have resulted in the practical disappearance of the former custom of drinking from a communal cup. As marks of their religious belief, Quakers and Dunkards wear special types of hats, while members of the House of David have no need for tonsorial services.

No attempt need be made to present a complete picture of religious customs or to trace their origin to establish the point that they exert a significant influence on human choice. To ignore this influence by assuming that these millions of people act merely from their reasoning as economic men in choosing goods and services essential to their method of worship might simplify the problem of explaining choice but would scarcely approach reality.

Christmas Celebrations. The customary celebration of Christmas is so closely related to religious customs that it is found only in countries professedly adhering to the Christian faith. Although less than half of the people of the United States are church members the custom of celebrating the anniversary of the birth of Jesus Christ is universal. December 25 is one of the first dates children learn. Indeed this celebration of Christmas has become so customary that in some cases it is merely perfunctory. There is a strong tendency for the economic aspect to overshadow the religious.

Real significance of the occasion is lost frequently in the acquisitive and customary exchange of gifts. Modern merchandising has seized upon this custom as upon others with the result that in the minds of many people the commercial aspect of Christmas is predominant. Trade papers are filled with news of the "Christmas trade," and economists in their study of cyclical fluctuations recognize its significance as a seasonal factor. A business amounting to approximately $5,000,000,000 annually in the United States is based on customary Christmas exchange of gifts. Eagerness to share in that business has led retailers to don their holiday decorations two weeks before Thanksgiving. There is no religious or church authority which requires the making or exchange of Christmas gifts. In fact the origin of the custom is difficult to trace, but it may bear some relation to the Christian doctrine that it is better to give than to receive. This is a plausible explanation, but it is doubtful if more than one out of a hundred could give any other reason for their practice than that it is simply custom.

The chain-letter fad breaks out unexpectedly from time to time to overload the mails. The customary practice of exchanging Christmas cards is somewhat in the nature of an annual chain letter fad which postal authorities accept and for which they prepare in advance. Throughout the year rhymers and ditty makers are busily engaged in preparing Christmas greeting cards which range from those which are really works of beauty with meaningful messages to those grotesque forms of pseudo art which fall in the realm of absurdity. The margin of profit in the Christmas card business is tremendous, yet the thought of composing an individual greeting card is one which rarely occurs to many people, for that is not the custom. It is feared that sending anything but a formal card which obviously costs from 5 to 25 cents would reflect unfavorably upon the sender's ability to pay.

The greeting-card custom has developed into a sizable business. In 1940 American manufacturers produced 2,400,000,000 greeting cards. This is equal to eighteen cards for every man, woman, and child. The total value of manufacturers' sales rose to $43,000,000 in that year. More than half of all greeting cards are sold at Christmas and at New Year's. Other dates responsible for large greeting-card volume are Valentine's Day, Mother's Day, and Easter, in that order. The heavy buyers of greeting cards are consumers in the income group from $1200 to $3500 a year. They buy 50 per cent of all the cards, while 37 per cent of the sales are made to consumers with less than $1200 yearly income.[1]

It would be interesting to know what proportion of the Christmas trade represents sheer waste. There can be no doubt that there are millions of people who give gifts to others not because there is an original, unrestrainable desire but because of custom, the desire to show off, or a sense of obligation. If people really wanted to give things to one another there certainly is no reason why they should wait for special traditional occasions. If a system of authoritative control were to forbid the exchange of gifts at Christmas time or any other such formal occasion, and permit only gifts made through a spontaneous desire so to express love or esteem, it is almost certain that the volume of goods so exchanged would dwindle, but that those actually exchanged would carry more meaning.

The perfunctory nature of choice which characterizes a large portion of the Christmas trade opens wide another avenue for waste. One need only mention the spectacle of a typical husband being advised by an inexperienced salesgirl in the selection of a suitable gift for a feminine member of his family. Ability of the buyer to pay is likely to be the determining factor in choice, rather than ability of the article to satisfy any possible want of the recipient. The buyer sets a price limit of one, five,

[1] *Business Week*, May 2, 1942.

ten, or any other number of dollars, leaving it to the ingenuity of a salesperson to discover "something that will do." Failure to meet even that simple test is revealed by the volume of post-Christmas exchanges and the still larger accumulation in millions of homes of unexchanged, unwanted, and unused trinkets.

Birthday Celebrations. Both American and European customs usually call for the celebration of the anniversary of the birth of each individual. Regardless of the economic status of families, each child is reared in a customary atmosphere which prescribes recognition of the event by a party and the presentation of gifts. A special custom has grown up which requires ice cream, cake, and candles for proper observance. Custom dictates that recipients of invitations to such affairs must present the honored guest with a gift. Here again perfunctory observance of custom results in a deluge of trinkets whose genuine utility is questionable. Another extensive custom is to send special birthday greeting cards to a friend or relative at the proper date each year.

Marriage Customs

As in the case of Christmas and birthday celebrations, an elaborate body of goods has grown up around the courtship, engagement, and marriage of men and women. Love of the opposite sex is one of the inborn tendencies which in practically all social groups culminates in marriage. Marriage customs are closely associated with religion and religious customs—so closely, in fact, that many people do not regard themselves as properly married unless the ceremony is performed by a clergyman in a church. On the other hand, our common law recognizes the act of a man and woman living together, and calling themselves husband and wife, as constituting marriage.

Courtship Customs. Methods of courting the favor of one sex by another are well established in all countries. It is customary, for instance, for the male to woo the female, although there is no particular reason why the method might not be reversed. Established customs of courting are largely carry-overs from European customs of long ago which regarded marriage as merely another form of business contract between two families, the terms of the contract being drawn by the father of the prospective bride and the father of the prospective husband. In those cases the actual participants often had little if anything to say about whom they would marry. Flaming youth frequently violated fixed custom and gave rise to practices still followed. Thus it is still customary for the young man in the case to seek the consent of the prospective bride's father, and in the marriage ceremony itself it is still customary for the father to go through the formal act of giving away the bride. The dowry

of former marriages has been largely replaced by modern legal division of the estate.

Engagement Customs. Modern engagements are vestiges of the former practice of signing and sealing formal contracts governing economic aspects of the approaching marriage. Formerly this was a contract of vital importance to the families as well as to the engaged couple. But the increasing tendency in this country is to regard the engagement as a contract between and affecting only the two parties. That an engagement has the binding force of a contract is demonstrated by the many successful lawsuits for breach of contract when an engagement is broken.

The engagement ring is an interesting example of a customary carry-over. In former days when most people were illiterate the method of signing and sealing a contract was to affix one's mark by the use of a signet ring. The ring has long been regarded as evidence of a contractual relationship. The signet ring of old has given way to the modern custom of wearing a diamond, a custom which serves admirably to sustain the diamond market. There are many young couples who deprive themselves of needed things by spending several hundred dollars on a diamond ring which cannot be afforded but which they feel must be purchased and worn by the fiancee for the sake of appearance.

Formal announcement of an engagement is usually the occasion for an elaborate party. With great solemnity the young lady's parents announce to the surprised world the approaching marriage of their daughter. Then follow a series of "showers" which bolster up the novelty business. There has been a noticeable tendency in recent years toward giving practical gifts on such occasions, but there still remains a high level of uselessness and sheer wastefulness.

The Marriage Ceremony. The type of marriage itself is a matter of custom. In this country a couple may be married by a representative of the church or by an official of the state. In other countries other customs prevail. In some countries economic necessity leads to the custom of polygamy or polyandry, but in the United States, as in Western countries generally, the influence of religion has led to the exclusive adoption of monogamy. While professing the virtues of that particular marriage custom, early Americans also insisted upon the value of a large family, especially one composed chiefly of boys who were economic assets in a country where labor was scarce.

Costumes worn at the bridal party are largely dictated by custom. It is said that some of our marriage customs are derived from the first Christians, who had been Jews. It was customary for Jewish brides to wear a gilt coronet, whose modern counterpart is an orange-blossom wreath. The use of orange blossoms is a customary carry-over from a

tropical clime whose people regarded them as symbolical of fecundity. The bridal dress also, together with the train, is a product of custom. Unlike the bride, the groom wears a costume that is determined by the hour fixed for the ceremony. In the morning he must wear striped trousers with no cuffs, a light vest, and a frock coat topped off with a special kind of cravat. In the evening he must wear the traditional full dress with black uncuffed trousers, white waistcoat, stiff-bosomed shirt with white tie, and black swallow-tailed coat. The only uncertainty as to the groom's costume is what constitutes proper attire for an afternoon ceremony. In the warmer months of the year there is no uncertainty even here, for custom requires white, cuffed trousers matched with white shoes, and a dark, preferably blue, coat.

In all these cases the power of custom is supplemented by that of emulation and the wish to consume conspicuously so as to display pecuniary power.

Marriage Celebrations. The customary feast is a vestige of the days when food supply was far less certain than it is at present. In its modern form it assumes the aspect of conspicuous display. The cake-cutting ceremony by the bride, with its distribution among her attendants, is a pretty custom which falls in the realm of superstition. Similar in its nature is the custom which requires the bride to toss her bouquet among her bridesmaids. Of course they are not her maids in the original sense of the term, but according to modern custom are her closest friends. The charivari is a noisy version of a custom dating from a chivalric period when uninvited friends serenaded the happy couple. Modern custom permits serenaders to continue their noisy pounding on cans and kettles until the bridegroom purchases their silence with suitable gifts.

The simulated escape of bride and groom provides a vicarious thrill for all members of the bridal party in lieu of the genuine excitement caused by the former custom of a groom stealing his bride from angry parents. In those days the chase was real and the best man had important duties to perform. The friendly throwing of rice and old shoes replaces the less friendly missiles of irate pursuers seeking to recapture the maiden. Rice, symbolical of fecundity, is thrown at the departing couple by well-wishing friends, most of whom in modern times are happily unaware of its real significance. The throwing of old shoes dates from the Israelite custom of removing a shoe in the presence of witnesses when closing a business deal.[1]

The honeymoon is a pleasant version of the ancient necessity of the bride and groom concealing themselves from earnest pursuers. Time was then reckoned by changes of the moon, and that one regarded as

[1] Wolff, Edwin, *Why We Do It*, The Macaulay Company, New York.

sweetest was properly called the honeymoon. In modern parlance it would more properly be called the sugarmoon. So deep-seated is this custom that at considerable sacrifice of other more important things modern bridal couples feel compelled to take a honeymoon trip in order to maintain their position and favor in the group. Wartime restrictions tend to alter this custom, but only temporarily.

Wedding Anniversary Celebrations. The power of custom over economic choice does not cease with the wedding ceremony or honeymoon. Within a year custom dictates observance of the first anniversay by presentation of paper gifts to the happy couple. Observance of this custom for the million couples married each year should provide a sizable market for paper-making industries. But these industries are not the only ones to enjoy economic gain through the custom of celebrating wedding anniversaries. The fifth year of marriage calls for wooden gifts, while the tenth is honored by tin or aluminum tokens. In none of these cases are the gifts regarded seriously by givers or recipients. The first really significant anniversary from an economic point of view is the fifteenth, which calls for crystal presents. This is followed by the twentieth, whose token is china, and the twenty-fifth, recognized by the presentation of silver gifts. To those couples who attain the fiftieth anniversary golden gifts are due, while that small number who enjoy seventy-five years of married life are honored with gifts of diamonds.

Since marriage and the family are basic social institutions which involve nearly all members of society, faithful observance of all or some of these customs by only a part of the group is economically significant. In passing through some of the most important experiences of life the economic choices of many persons are determined not by themselves but by that illusive, pervasive force called custom.

Burial Customs

In the different countries of the world today, the customary ways of disposing of the dead are profoundly influenced or determined by religion; but they vary greatly. In some densely populated regions it is not surprising that cremation is the rule, for very little land could be spared for cemeteries.

In the United States in recent years the number of cremations has increased considerably, but the great majority of the 1,400,000 dead each year are interred in cemeteries or in mausoleums, with funeral and burial expenses much greater than in other countries. The results of a survey may be summed up as follows: For those whose estates amount to $1,000,000 or over the average general expense is $3,075, two thirds of which is spent for burial lot, monument, flowers, and other extras. For

those whose estates range from $1,000 to $5,000 the average expense is $541, while those who leave less than $1,000 have an average of $372 spent on their burial. In Brooklyn burial expenses absorb 62 per cent of estates below $1,000.[1] The average annual business of undertakers amounts to $400,000,000. This is supplemented by an annual volume of business amounting to $60,000,000 for florists and $40,000,000 for monument makers.

Reduced to relative terms, the high cost of living is very small as compared to the high cost of dying. The culmination of a lifetime of unsound consuming standards is the customary standard of burial. Popular belief that the highest final honor is that of a state burial is an ironic contrast to the equally popular belief that the crowning indignity of life is state burial for the pauper. The importance which society places upon a "decent" burial is indicated by the laws in at least half of the states which give burial charges precedence over all other claims against the estate of the deceased.

In earlier times in this country, before about 1875, burial services were far less expensive. It was about 1875 that the modern practice of embalming was introduced, and industrial insurance was originated as a means of providing the several hundred dollars needed for a "decent" burial. The latter innovation proved very successful in supplying millions of lower-income people with a cash fund to cover burial expenses. In 1937 there were 88,900,000 industrial insurance policies in force—covering approximately 50,000,000 persons—with an average value of $233.[2] The burial cost for these people ranged from $194 in North Carolina to $484 in New Jersey. The average was $363, or $130 more than the average insurance carried. This surplus remained as a debt against whatever estate was left, or had to be assumed by surviving relatives.

Leaders of the funeral industry themselves attribute part of the high cost involved to the lack of organization in the industry. Believing that unusual profits were to be obtained, more than 34,000 men have gone into the funeral business. From 1900 to 1920 the number of undertakers increased twenty-five times as fast as the increase in volume of business. London has 800 undertakers, compared with 2,000 in New York. That the industry is much overcrowded in the United States is further demonstrated by the fact that the number of funerals per firm shrank from 194 a year in 1880 to 51 in 1930. Leaders of the industry estimate that only

[1] Advisory Committee on Burial Survey, *The Reasons for Present-Day Funeral Costs*, p. 11. This study, under direction of John C. Gebhart, was financed by the Metropolitan Life Insurance Company.

[2] Temporary National Economic Committee, *Study of Legal Reserve Life Insurance Companies*, Monograph No. 28, p. 248, United States Government Printing Office, Washington, D. C., 1941.

23 per cent of the funeral employees' time is used in their work; as a result 77 per cent of their time is wasted.

Proponents of a burial association plan contend that it is natural and logical for one to anticipate death by providing in advance for one's own burial at a price agreed upon in circumstances such as surround any other business transaction, in contrast to the highly emotional state in which survivors commonly make necessary business arrangements with the undertaker. It is their contention also that most of the extra costs due to the greatly varying number of deaths per week can be overcome by a large association; by guaranteeing an undertaker 100 funerals a year the cost of each service could be reduced from $133 to $99. According to the testimony of one witness, the actual cost of the average private funeral is $98, while the price ranges from $200 to $500.

By guaranteeing 100 funerals to an undertaker a burial insurance company secures wholesale prices which run as much as 30 or 40 per cent under the retail price. A funeral which retails at $250 can be bought by the insurance company for $150; a $400 funeral can be bought for $250, and a $500 funeral for $350.

Broadly speaking, our method of disposing of the dead is unnecessarily expensive. From the standpoint of human welfare, many believe that the half billion dollars or more spent every year is largely wasted. Disposition could be made in an effective, dignified manner for a fraction of the present cost. Why does the great expense of funeral services continue without much opposition? Partly because the mystery of death is shrouded in a mixture of emotion, religion, and awe; and partly because of the influence of those who profit through a continued blind devotion to custom; and largely because of the dictates of custom and its influence over the individual consumers, who prefer to pay large bills rather than risk the disapproval of their friends. There is not much reason to believe that rationality will ever displace custom in this sector of human life. Yet there is a great possibility for modern youth to start a crusade to strip burial practices of false standards which, if they do not detract from human welfare, certainly do not contribute to it.

Ceremonial Customs

Holiday Celebrations. Customary observance in the United States of July 4, Thanksgiving Day, and other national holidays carries with it practices possessing economic significance. Set aside originally as an anniversary celebrating the American Declaration of Independence from Great Britain, July 4 has become a day whose customary observance partially supports the manufacture of miniature munitions. Here is a striking illustration of positive disutility and waste. The scores or hun-

dreds of boys and girls annually killed or maimed by fireworks have no original desire for these products. Children of other nations celebrate their anniversaries of independence in less disastrous and more effective ways. If the time ever comes when this crude custom is abolished, children of future generations will not constitute a market for such illth.

Originating as a day of thanksgiving to God for a supply of food sufficient to carry the Pilgrims through the following winter, Thanksgiving Day has so far fallen under the influence of custom that its modern observance requires a sumptuous and expensive banquet. Because wild turkeys happened to be available in New England, modern givers of thanks demand turkeys. As a result these birds have become domesticated and are reared in large numbers. A few independent souls who prefer chicken or duck, or even beef or mutton, are likely to find their children harboring a feeling of embarrassment, chagrin, or resentment at their failure to observe the Thanksgiving Day custom properly.

Customary Ceremonies. A significant body of custom has grown up around such events as the opening and closing of legislative bodies and the inauguration of executive officials in public life. While this is more true in countries retaining royalty, evidences of its influence are observable in American life. Thus the inauguration of a governor or a President calls for an elaborate ceremony and program and the wearing of clothing sanctioned by custom. For such an official to assume office not properly attired in morning dress with stand-up collar and top hat would be regarded by many as ominous.

In private life similar ceremonial customs prevail in lodges, fraternities, and other secret societies. An elaborate ceremonial ritual is supplemented by still more elaborate regalia, badges, pins, and insignia. These latter requirements constitute a large market for jewelry firms and costumers catering to such trade. No matter how one may explain the origin of such organizations, the significant fact for our purpose is that demand for such commodities does not emanate from individuals, but from groups which are powerfully influenced by custom.

Graduation Exercises. Certain curious customs have developed in connection with the passing of students from grammar school to high school, from high school to college, and from college to life. In addition to ceremonial programs and speeches, graduation exercises require special ceremonial dress for the college graduates. When, in the reign of Edward III, Englishmen eliminated from their costume hampering flowing robes, these were retained by lawyers, jurists, and educators as marks of distinction. The modern academic cap and gown, whose cost in the case of higher collegiate degrees may amount to as much as $100, is a customary vestige whose sole purpose is to set off the wearer from his

more humble fellows. At the time of the Italian Renaissance students in Italian universities were required to wear the scholar's gown. This was mainly for their own protection since it served notice to all who could see that the wearer was a student at a university and therefore in a special class insofar as the laws of the country were concerned. The statutes of Italian universities required their students to wear the long, black garment called the *cappa*, one of the reasons being to limit the cost. The gown, woolen for winter and linen for summer, gradually grew longer until it came to the heels. "A person who was entitled to the hood of the academic dress wore it also and cherished it . . . To snatch away a scholar's hood was considered an intolerable insult, . . . "[1] It is interesting to observe that no such costume is now customarily worn by graduates from grammar school nor even by high school graduates. This may be due in no small part to the fact that American educational laws require all children to complete grammar-school education, and that more than half of them continue their education also through high school. There is consequently little distinction in being one of 22,000,000 attending public schools; but those fortunate few comprising about 1,350,000 who are able to attend college must needs set themselves off in special costume, when graduating, so that all who see may know. But even this desire for distinction would not lead to an individual demand for such regalia in the absence of long-established custom. Recently students at a well-known college successfully rebelled against academic costume. Perhaps this marks the beginning of a new and less expensive custom.

An interesting part of graduation customs is that of bearing gifts to those who have completed their course of study. In former days these tokens of admiration were fairly simple and inexpensive in the case of high school graduates, but the modern tempo encouraged by advertising has stepped up the standard until it becomes a real burden to those who have numerous nieces and nephews. While the customary gifts are usually possessed of genuine utility, the modern tendency is toward the inclusion of trinkets and gadgets whose usefulness is open to question.

An important by-product of graduation exercises and ceremonial customs in general is the photograph. Extremely valuable in its proper sphere, the custom of photographing individuals and groups in connection with ceremonial occasions has become an important adjunct of the photographic industry.

Private Parties. The whole realm of private entertainment is colored and continued by custom. The desire of man to be with his fellows is a

[1] TAYLOR, R. Emmett, *No Royal Road*, pp. 147–148, University of North Carolina Press, Chapel Hill, North Carolina, 1942.

normal result of the gregarious tendency, but custom, emulation, and conspicuous consumption foster and expand much artificial social life. From elaborate state dinners featuring public life, down to dinners in the lower-income groups, the power of custom fosters a sense of social obligation which alone explains the elaborate entertainment of persons for whom the host may harbor a feeling of positive dislike. Economic aspects of this phase of custom are far-reaching. The President of the United States is allowed $25,000 a year for traveling expenses and formal entertainment, an amount which is usually inadequate. American diplomatic representatives abroad frequently spend more on formal entertainment than they receive as remuneration. The apparently liberal salaries of Congressmen are substantially reduced by this expensive custom. In private as well as in public life conspicuous display and emulation play an important part, as will be shown in subsequent chapters.

Operation of these same forces is observable in the social life of smaller-income groups. While it is difficult to draw a line between entertainment emanating from a genuine pleasure in association with friends and that originating from customary practice, operation of the latter influence is undeniable. Variations in practice among economic classes represent differences in degree. In all cases the expenditure of wealth reflecting concrete economic choice results in large part from custom. A genuinely economic man would, as some do, entertain only those from whom some economic gain could reasonably be expected.

Summary

Customs are strongest in those sectors of life closely related to human emotions. Religious customs are numerous and deep-seated, powerfully affecting the character of consumer choice. Of the same type are customs associated with Christmas and individual anniversary celebrations. From courtship to golden wedding anniversary, marriage customs color economic choice. Burial customs are responsible for needless expenditures for goods and services which do not satisfy an original human desire. Other custom-made expenditures are for Independence Day, Thanksgiving Day, graduation exercises, and private parties.

Analysis of modern customs leads to the conclusion that many are harmless and unimportant. With these there is no cause to be concerned. There are other customs, however, which interfere seriously with the promotion of human welfare. Against these, courageous consumers must constantly be on the alert. When a custom ceases to serve a useful purpose, rational consumers can expand their freedom of choice only by asserting their independence of false constraints.

QUESTIONS FOR DISCUSSION

1. What is your reaction to ceremonial worship?
2. To what extent are your personal economic choices determined or influenced by your church affiliation?
3. What special economic goods, such as communion cups, are produced in response to a religious denominational demand?
4. On the basis of your observation would you say that ceremonial practices in worship, marriage, and education are increasing or declining?
5. Why should Christmas be a day for exchanging gifts? Contrast the religious with other motives tending to perpetuate the practice.
6. How do you celebrate Thanksgiving Day? New Year's eve? Why?
7. How many Christmas cards to you send? Do you buy them or make them? Estimate the number sent by fellow students on your campus and then estimate the total expenditure.
8. Evaluate courtship and marriage customs in terms of consumer welfare. To what extent will your economic choices be influenced by these customs?
9. To what extent are your current economic choices affected by traditions at your college? By your sorority, fraternity, lodge, or club?
10. When you graduate will you wear an academic gown and cap? Why?

PROBLEMS AND PROJECTS

1. Visit several different churches to observe and compare their ceremonial practices. Interview the bishop, priest, or rector to discover if possible the origin and significance of some of the customs.

2. Make a study of one of the major religions to ascertain the extent of religious influence on economic choice.

3. Interview the merchants of your town or officials of the Chamber of Commerce to secure their estimate of the volume of business accredited to Christmas buyers.

4. Write a report contrasting marriage customs of Catholics, Hebrews, and Protestants; emphasize their effect on economic choice.

5. Interview at least two undertakers. Secure as much information as you can as to annual number of funerals, average cost of each, cost of embalming, cost of casket, etc.

6. Ascertain the number of casualties in your state as a result of celebrating the last Fourth of July with fireworks. How many people in your state celebrated last Thanksgiving Day by attending football games? How much was paid for admissions?

7

Choosing Goods for Display

CONSPICUOUS CONSUMPTION

Among forces influencing individual choice is that curiously significant urge to possess and consume wealth for the sake of display. A generation ago Thorstein Veblen revealed in his inimitable style the operation of this force, which he called conspicuous consumption. This may be defined as the consuming of wealth and services on a grand scale for the purpose of demonstrating pecuniary power rather than to satisfy an organic or cultural want. Its very essence is waste rather than utility.

J. A. Hobson reaches essentially the same conclusion in his analysis of what he regards as the three factors affecting the standard of living. Economic choice for such basic commodities as food, clothing, and shelter is determined by what he calls the primary organic factor. A second conditioning force is the industrial factor, which determines the choice for certain goods on the basis of occupational activity. It is in the operation of conventional forces upon consumer choice that consuming for display appears. In Hobson's judgment the conventional factor is the most important of the three and the one which opens wide the door to waste. There can be no doubt that when conventional display displaces the primary organic and industrial factors as determinants of choice a wide margin of waste appears.[1]

ORIGIN AND DEVELOPMENT OF CONSPICUOUS CONSUMPTION

In Primitive Life. In primitive tribal life conspicuous consumption is found as a form of class distinction, based, however, on physical power and prowess rather than pecuniary power. The braves reserved for themselves certain forms of consumption which were denied to lesser men and to women. Only those who had achieved distinction in the hunt and on the battlefield were permitted to enjoy certain luxuries. A common restriction was that which denied the use of intoxicating drinks to all but the mighty. A similar restriction was that which reserved the privilege of smoking to a small circle of men. The choicest morsels

[1] HOBSON, J. A., *Work and Wealth*, chap. 10, The Macmillan Company, New York, 1914.

of food, the most desirable skins, and the most beautiful feathers were appropriated for their exclusive use. A curious result of these practices was that certain diseases attributable to overindulgence were considered honorific and in themselves brought satisfaction to the sufferer. In this way gout early became a disease of distinction, proclaiming to all the world that the victim had been free to indulge his every whim. In the same way drunkenness, instead of being condemned, became a means of honorific and conspicuous display.

In Medieval English Life. As economic life changed, bringing in the use of money and its acquisition as a measure of success, consuming standards were gradually altered to meet new conditions. While the wealth of England in the fourteenth, fifteenth, and sixteenth centuries was much greater than that of tribal groups it was still comparatively limited. Persons of wealth were limited in their efforts at display to the purchase of land, erection of palaces, wearing elaborate clothing, and consuming inordinate amounts of food.

Competition in conspicuous dress so seriously threatened to break down existing caste lines that in 1325 William of Malmesbury claimed "that the squire endeavored to outshine the knight in the richness of his apparel, the knight the baron, the baron the earl, the earl the king himself."[1] This led to repeated but usually futile efforts to regulate the clothing of individuals so that their station in life might be apparent to all. Sumptuary laws were not confined to clothing, but carried over into the realm of food. There were rigid regulations setting forth types of food and number of courses for individuals according to their social position.

In the reign of Richard II "luxury and ostentation became a feature in the life of nearly all classes of the nation." Still later, under Henry VI, "many absurd, fantastic, or extravagant styles reached their height. . . . It was a time of lavish display, surpassed in quaintness, color and variety by the time of Henry VIII." Under Queen Elizabeth the magnificence of mansions, dress, and entertainments of the nobility and gentry surpassed anything that England had previously known, with Elizabeth herself a mirror of fashion and a mold of form possessed of a wardrobe of 2,000 dresses.[2]

The uselessness of conspicuous dress is revealed in the writing of Joseph Strutt, describing the apparel of men servants who copied their master's dress. They had "such pleytes upon theyr brestes and ruffles upon theyr sleeves above theyr elbowes that, yf theyr master or them-

[1] BALDWIN, Frances Elizabeth, *Sumptuary Legislation and Personal Regulation in England*, p. 21, vol. 44, Johns Hopkins University Studies, Baltimore, 1926.

[2] *Ibid.*, pp. 88, 194.

selves hade never so great neede, they could not shoote one shote to hurt theyr enemyes, tyll they had caste of theyr cotes or cut of theyr sleeves."[1]

As the amount of wealth increased and its distribution among members of the group continued to be unequal, a single individual could not himself consume his entire income. Thus a retinue of hangers-on became an effective means of display of pecuniary power. In order that everyone might know that these hosts of servants were dependent upon the master for their very existence they were placed in liveries. Originally the word livery referred to the allowance of food dispensed to a family, and it later acquired an added meaning of a gift of clothes made by a master to his servants. In 1448 the Earl of Warwick was followed by 600 liveried servants in his conspicuous procession to Parliament. This so aroused the jealousy of others that new sumptuary laws were passed to prevent such elaborate display by a mere earl.[2]

In Modern Life. Modern illustrations of this type of conspicuous consumption are not difficult to find. Among those whose names appear in the social register, maintenance of a retinue of servants elaborately garbed in livery, bearing the insignia of the master, is considered not only fitting and proper but absolutely essential. The question may very properly be raised as to what possible utility is to be derived either by master or by servants in the wearing of livery. If there is any other purpose than to advertise to the world the wearer's dependence upon his master and to distinguish him from his master it has never been revealed. In this connection it is interesting to observe that while butlers, chambermaids, and chauffeurs are invariably required to wear uniforms, for which they must usually pay, grounds keepers, kitchen servants, and others less likely to be observed in public are for that reason less frequently garbed in distinctive livery.

Indignation of "English upper classes" over competitive emulation by "inferiors" is matched by that of contemporary persons whose chief complaint in life is against the presumption of those in lowly estate who dare to dress in a grand manner. How frequently one hears the complaint that an employer's stenographer is garbed in silk stockings, smart frock, and fur coat that cannot be distinguished from his wife's clothing! If there is any reason why her clothing should be distinguishable it is simply to enable the employer's wife to help him display his greater pecuniary power. In the same vein complaint against workingmen owning and driving automobiles is frequent. If it were possible those of greater means would arrogate to themselves exclusive use of that modern means of transportation. Since the industry has developed low-price cars, their only refuge is to buy expensive limousines.

[1] BALDWIN, *op. cit.*, p. 136.

[2] *Ibid.*, p. 73.

This feeling of resentment is even carried so far as to cause many people to criticize severely the consumption of certain foods by more lowly persons. The old complaint that the squire cannot be distinguished from the lord is still prevalent. Many modern money lords would welcome the power of their ancestors to regulate by law food which others might eat, clothing they should wear, the kind of houses in which they should live. Only by such means could such false standards of superiority be rendered more secure.

As the volume and variety of wealth have continually increased, opportunities for conspicuous consumption have increased. With the development of commerce among nations, delicate, expensive foods became available as a mark of consuming distinction. Foreign products became superior because they were expensive and therefore not available for those of limited means. Those who disdain such common fish as sturgeon speak in a superior tone of their preference for Russian caviar, blissfully unaware of the fact that the supposedly choice morsel is nothing more than the prepared roe of sturgeon.

The dinner service early assumed importance as a means of conspicuous display. Royalty and near royalty must have found that food tastes no better when served on a golden plate than when served on a piece of china, but the fact that they could use golden service satisfied that other longing to demonstrate their superiority. Even among royalty there were differences in pecuniary power. Some had to be content with golden plates, while others were able to prove their superior power as potentates by supplying themselves with jeweled gold service sets. The sultans of Turkey used plates so heavily bejeweled that it must have been difficult to separate food from jewels. For those below the rank of royalty dinner sets of plated gold or gold-rimmed dishes had to suffice to mark their relative superiority over those still further down the scale. Next in line were those qualified to use sterling-silver service. In recent years certain sterling silverware manufacturers have felt that the automobile has largely replaced sterling silver as a mark of social distinction.[1] Going on down the scale one finds imported china, cut glass, and plain pottery dishes to mark the relative economic position of the owner. While the economically unimportant can eat and enjoy their food in one serving, their self-appointed superiors find a seven-course dinner an effective means of display, even though it may not add to their enjoyment.

Judged by standards of conspicuous consumption, certain types of clothing which indicate their unsuitability for manual labor acquire added utility. The man who arrives at his office at nine o'clock, attired

[1] Borden, Neil H., *The Economic Effects of Advertising*, p. 203, Richard D. Irwin, Chicago, 1942.

in spotless gray with white collar and light gloves, proclaims to the world that he is not required to perform menial manual labor. By the same token, the man who appears on the street at 11 o'clock in formal morning dress of striped trousers, frock coat, and top hat proclaims to all who see that he does not even have to do office work. Regardless of whatever other satisfaction his clothing may yield, it enables him to tell the world that he is a gentleman of leisure.

In some respects women have not advanced far beyond the days when they were regarded as slaves and suitable trophies of war. Now, as then, they may be used conveniently by the wealthy master as show windows for conspicuous display. Even more so than in the case of men, the clothing of such women is carefully designed to make it perfectly evident that the wearer could not possibly have to do any kind of work. Not only the designs but the very materials have been chosen with that end in view. Hoops, hobble-skirts, corsets, high heels, and bell-shaped sleeves have all been designed for essentially the same purpose.

Inadvertently the liveries of servants serve a similar purpose. The nattily attired chauffeur is obviously improperly attired for driving a garbage truck. A nurse in white uniform and a butler in livery are obviously incapacitated for what they regard as menial tasks. In this connection it is interesting to learn that rigid caste lines exist among servants, patterned after the lines of their masters. If the lady of the house is concerned about the order of seating for her guests, servants in their quarters are no less concerned. An Englishwoman of wealth has told of this example: One of her menservants asked to be allowed to change his seat at the table so as to be near one of the maidservants whom he expected to marry; but Thomas, the butler, denied his request because it would disarrange the seating of the group according to their relative rank.

The house has long since ceased to serve only as a shelter from the elements. The wealthy man's house has also passed far beyond the realm of comforts, into that of superlative luxury as a means of conspicuous display. The house itself is made of splendid and expensive materials, all or many of which are probably imported from distant countries. Decoration, equipment, and hangings are elaborate and ornate. In the house of a certain Pennsylvania millionaire solid gold doorknobs and solid gold bathroom fixtures demonstrate beyond any doubt the enormous pecuniary power of the owner. The size of such houses is beyond all practical need. A family of three or four would be put to it to make any genuine use of a 142-room mansion. The unused space in it does serve, however, not only to demonstrate the owner's consuming power but also to house admiring emulators and envious competitors. In addition to the main mansion there are of course quarters for the servants,

each indicating by its size and elegance of decoration the relative rank of the occupant.

The 2,000 or more acres of land comprising what is known as the estate are carefully planted with grass, shrubbery, and flowers through which run alluring walks and bridle paths, all of which demonstrate forcefully the owner's ability to withhold from productive use such vast domains. To own such extensive acres and be able to withhold them from use is itself evidence of wealth. To go one step farther and actually use the land in such a way as to incur additional expense is evidence of even greater pecuniary power.

Private greenhouses serve not only to supply the mansion with out-of-season cut flowers, but to bring repute to the owner in the form of prizes and publicity for winning entries at flower shows. In addition to an elaborate array of recreational facilities, including swimming pool, tennis courts, and a private golf course on or near the estate, a really complete display of monetary power requires the maintenance of a stable of racing horses. Appearance of these animals at classic turf meets is an effective means of subtly suggesting to thousands of onlookers the tremendous wealth which the owner must control.

As the standard of conspicuous consumption is raised, possession of one of these mansions with its retinue of servants becomes inadequate to demonstrate conclusively the superior consuming power of the owner. A real modern American potentate must have a town house, a suburban estate, a home in the mountains, another at the seashore, and finally a Florida or California retreat. On the other hand, an English author describes the extent to which people of moderate means sometimes go to create the impression of possessing great wealth. She tells of a family that lived in great style in London in the winter. Their house was situated in a fashionable neighborhood, was maintained by a retinue of servants, and was the center of a gay social life. In summer, however, the house was closed and while the family ostensibly went to their country home they actually moved to another section of the city, where they lived in three back rooms, subsisting on tea, toast, and eggs. All the servants were dismissed, and the elaborate carriage dispensed with. Mail was directed to a fashionable country address and from there forwarded to their actual residence.[1]

In America a striking example of the display of real pecuniary power has been provided by William Randolph Hearst. Inheriting the 40,000-acre estate called San Simeon, he enlarged it many times until it extended more than fifty miles northward from Hollywood along the

[1] Peel, Mrs. C. S., *A Hundred Wonderful Years*, p. 86, Dodd, Mead & Company, New York, 1927.

Pacific shore line. Triple gates manned by liveried porters guarded the entrance to the Spanish castle wherein the owner dwelt. Numerous "cottages" resembling chateaux provided separate suites for the many guests often enjoying his lavish hospitality. Riding, tennis, and swimming apparel were provided for guests who did not bring such equipment with them. Three swimming pools, one containing warmed sea water, were at their disposal. Riding, hunting, and tennis offered leisure entertainment. Most of the guests were transported in automobiles, but some important persons were flown from Hollywood in one of the private planes. On one occasion a sudden impulse to go to Europe led Mr. Hearst to invite his threescore guests to go with him on his private yacht. On the great estate, in addition to poultry and dairy farms and botanical gardens, the owner maintained a private zoo; also a private museum to house his collections. In addition to a collection of armor said to be the finest in the world, Mr. Hearst also has collected silverware, paintings, pottery, tapestries, costumes, choir stalls, and fireplaces. Other fine collections of his are housed in residences in and near New York City. The annual expense entailed by all this conspicuous display has been estimated at $15,000,000.[1] But the Hearstian penchant for conspicuous display, by 1942, was on the decline. San Simeon was for sale and portions of the various collections had already been sold.[2]

The joining of the Cromwell and Duke fortunes by marriage is described in a popular periodical which also provides a striking illustration of current conspicuous consuming for display. Duke Farms at Somerville, New Jersey, is a 2,400-acre estate with 42 miles of paved private roads. There are other estates at Rough Point, Newport, Lynnewood, in North Carolina, Antibes, and Palm Beach. The newest addition is Shangri-La in Hawaii, to which the Cromwells commuted by Clipper plane. Cromwell's mother-in-law has a marble mansion on Fifth Avenue in New York, while his mother had, until recently, Whitemarsh Hall, a 142-room house in Philadelphia, Wingwood House with its 90 rooms at Bar Harbor, El Mirasol at Palm Beach, and a 20-acre estate on the edge of the nation's capital.[3]

Lest it be thought that these are exceptional illustrations, let us turn to the findings of a market survey made by the publication *Town and Country*. Unable to get information from the wealthy people directly, the following facts were obtained by means of a questionnaire from the members of The Butler's Club of New York with a membership of 2,000.

[1] Carlson, Oliver, and Bates, Ernest Sutherland, *Hearst, Lord of San Simeon*, chap. 20, The Viking Press, New York, 1936. [2] *New York Times*, June 28, 1942.

[3] Alexander, Jack, "Golden Boy, The Story of Jimmy Cromwell," in *The Saturday Evening Post*, March 23, 1940.

One hundred butlers supplied the following cross-section: Of the Vanastorbilt families, 94 per cent have each a country house with an average of 22 rooms. Most of them, 87 per cent, have town houses with an average of 18 rooms. There are five members in the typical Vanastorbilt family, with 11 servants on the average, although the range is from 2 to 40. The Vanastorbilt family owns, on the average, three automobiles and entertains 181 people every month during the summer, dropping off to 138 guests a month during the winter. To quench the thirst of these guests the Vanastorbilts purchase 2,400 bottles of liquor every year. When not entertaining, the Vanastorbilts like to travel at least two or three times a year to such spots as Maine, White Sulphur, Florida, California, Nassau, Bermuda, and Europe. On each trip they take one or two servants and manage to get along with seven trunks.[1]

Contemporary Forms of Conspicuous Display

Travel. Ingenuity of modern men has created additional effective means of conspicuous consumption. The standards of living of modern money kings possessed of hundreds of millions of dollars' worth of wealth put to shame the standards of display of royalty in former times. Indeed there are few contemporary monarchs who enjoy incomes equal to those of many American magnates.

Wealthy Americans are constantly put to it to discover new and dazzling means of impressing their fellow men with their regal power in economic life. Domestic and foreign travel is in itself an effective means of displaying wealth and leisure; but the relative extent of one's power is better revealed by the type of transportation used. An ordinary automobile of American manufacture would serve no other purpose than that of providing efficient transportation. Consequently an imported car, costing $15,000, is purchased, to serve the double purpose of providing transportation and conspicuous display. For the use of all members of the retinue other than the master, a fleet of lesser cars is maintained. Modern standards of reputability permit the inclusion of a Ford service car on large estates.

Recent progress has brought a still more effective means of transportation in the airplane, which serves the dual purpose of providing fast conveyance in a conspicuous manner. While the prerogative of air transportation is still largely limited to persons of wealth, it is a superior mark of distinction to own a private plane and in spite of the popular admiration of those capable of flying planes it is already an additional mark of superiority to be able to count a private pilot in one's retinue of servants.

[1] *Business Week,* March 18, 1939.

A seashore mansion is incomplete without an expensive yacht. The prewar social register listed the names of 1,500 owners of yachts whose cost ranged from several hundred thousand dollars to four million. These vessels are capable of traveling the seven seas and demonstrate the owner's ability to travel even more expensively and luxuriously than would be possible in first-class quarters of the latest transatlantic luxury liner.

A fourth common mode of travel is by train. While coaches are good enough for common people, Pullmans are required by those in the class immediately above, compartment cars by those still farther up in the economic scale, private cars by those next in line, and private trains are reserved for modern masters.

Sports. In order to secure approval of his group the so-called modern gentleman must be proficient in sports. The prestige of sports is a carry-over from primitive days when men lived by their skill and cunning. The genuine gentleman must be skilled in forms of recreation which not only fail to yield an income, but which entail an expense which closes them to all but the wealthy. Included in this category are polo, boat racing, and to some extent golf and tennis. Increasing participation by people of lesser incomes in the latter two games is rendering them less satisfactory as means of effective display. A curious custom is that which not only condones but requires the ownership of a stable of racing horses by the master of an estate, and yet frowns upon his riding a horse in competition. The thrill of the chase is simulated in modern elaborate hunts which require a costume of brilliant hue, a string of horses, and a kennel of hounds.

Lavish Entertainment. The part which custom plays in supporting the social amenities has already been observed. Entertainment on a lavish scale goes beyond this customary observance in affording a means of displaying pecuniary power. It serves the additional function of humbling competitors in the very presence of those who are most likely to be impressed. Week-end parties, coming-out parties, engagement announcements, and marriages afford convenient means of lavish and patronizing entertainment.

Philanthropy. Under an economic system which not only permits but encourages extreme concentration of wealth, an offsetting factor in public opinion is the philanthropy of the rich. A difficult, alluring question which cannot be discussed here is whether the millions of dollars annually disposed of by these so-called public benefactors yield more or less utility than they would if appropriated by taxation and expended by the state.

The significant observation for present purposes is that there is very

little anonymous philanthropy. This simple fact seems to justify the conclusion that public applause and admiration for the powerful wealthy are in many cases among the mixed motives lying back of such private sharing of wealth. The name of a wealthy donor is used for the name of a great college or university or benevolent institution dispensing millions of dollars. For those who cannot afford more lavish displays of wealth, public recognition may always be achieved on a smaller scale by means of donations to any one of the several hundred struggling colleges throughout the country. It is no mere chance that so many of those institutions bear the name of a contributor to their endowment or that practically all college buildings are known as halls, each with the name of the chief benefactor deeply cut in a conspicuous stone.

While churches rarely use the name of their chief benefactor there are various means for letting members of the congregation know who are the chief supporting pillars. Far beyond the confines of New York City the name of Riverside Memorial Church is inextricably linked with that of John D. Rockefeller. Lesser lights secure recognition through memorial pews, pulpits, and stained-glass windows.

Higher Education. For many consumers of educational facilities beyond high school graduation, the element of conspicuous consumption is not an unimportant consideration. As a country grows older and the number of first families increases, a perfunctory form of so-called higher education becomes essential to maintenance of caste. In most college classrooms one will find some students who are there simply because it is being done.

Once enrolled, the type of course studied may itself serve the purpose of conspicuous consuming. A college degree carries prestige, but among some people a cultural education resulting in an A.B. degree carries even greater prestige by its implication that the possessor is free from the necessity of working and enjoys an independent income. The less practical the courses the better they serve the purpose of such students. Those few who can render a public address in Latin enjoy a prestige similar to that enjoyed by the proud owner of a four-million-dollar yacht. In the judgment of Mr. Hobson it is probable that

> "Our higher education, properly tested, would be found to contain a far larger waste of intellectual 'efficiency' than our factory system of economic efficiency. And this waste is primarily due to the acceptance and survival of barbarian standards of culture, imperfectly adjusted to the modern conditions of life, and chiefly sustained by the desire to employ the mind for decorative and recreative, rather than for productive or creative purposes. Art, literature and science suffer immeasurable losses from this misgovernment of

intellectual life. The net result is that the vast majority of the sons and daughters even of our well-to-do classes grow up with an exceedingly faulty equipment of useful knowledge, no trained ability to use their intellects or judgments freely and effectively, and with no strong desire to attempt to do so. They thus remain or become the dupes of shallow traditions, or equally shallow novelties, under the guise of scientific, philosophic, economic or political principles which they have neither the energy of mind nor the desire to test, but which they permit to direct their lives and conduct in matters of supreme importance to themselves and others."[1]

Academic degrees and costume serve conspicuous consumers of higher education admirably by providing them with the distinctive mark of a cultured gentleman. For those who cannot earn such degrees in the usual way there is the convenient practice of awarding honorary degrees to munificent benefactors.

Conspicuous Consumption of Inherited Wealth

Inherited Wealth Yields Greater Prestige. An interesting development in the psychology of conspicuous consumption is that which attaches especially great prestige to the dispenser of inherited wealth. As the social group gains maturity the position of those who inherit their wealth is more firmly entrenched than that of those who are compelled to acquire it. The former, having been reared in a grand manner, have learned as a matter of course how to consume wealth conspicuously without appearing to do so. Standards of the second and third generation require the art of consuming decorously. There are some cartoonists who have made their own fortunes by depicting the struggles of newly rich to crash the portals of this supercaste.

After all it must be admitted that the first wealthy Morgan, Ford, Rockefeller, Astor, Vanderbilt, and Harriman, to mention only a few founders of family fortunes, did engage in productive enterprise. They were so busy laying the groundwork of their fortunes that they had little time or inclination to consume conspicuously, certainly not to the full extent of their power. Their satisfaction and distinction lay in their ability to acquire huge fortunes. The full power of prestige carried by those fortunes was reserved for children and grandchildren.

A curious condition results when, as sometimes happens, individuals inherit gentility without wealth. The former plantation system of the South resulted in some such cases, but they are much more common among the nobility of the Old World. As these poor men have been born

[1] Hobson, J. A., *Work and Wealth*, p. 153. By permission of The Macmillan Company, publishers.

to the blood, others more favored by fortune find a double satisfaction in adding them to their retinue of hangers-on by giving them sinecures with such a high-sounding title as "Keeper of the Kennels."

Conspicuous Consumption in Middle- and Lower-Income Groups

Desire for Display Is Universal. In the preceding discussion emphasis has been placed upon those favored few who possess large fortunes. In the illustrations which have been given there have been, however, numerous allusions to the practice of conspicuous consumption among those lower down in the pecuniary scale. It is now time to state positively that conspicuous consumption is by no means limited to the very wealthy. It permeates all income groups, differing only in degree.

In contrast with those whose wealth is inherited, men who have to work for a living place the full responsibility for conspicuous consuming upon their wives. It might be added parenthetically that the latter seem usually to accept that responsibility eagerly. The wife of a small-town businessman is more than a wife, mother, and housekeeper. Together with the family home and automobile she serves to demonstrate largely by means of her clothing the relative pecuniary power of her husband.

In all groups, of course, conspicuous consumption leads to competitive consumption. Whether among the four hundred or among a college faculty group there will be gradations in income, making it impossible for all to consume on the same scale. No matter how far down in the procession a family may be, there is usually a determination to put its best foot forward as far as it can. Even among the immigrant class the urge to attract attention by putting on a conspicuous display of wasteful consumption at least once in a lifetime is shown in elaborate weddings and funerals so typical of that class. "The great object in life is social position. To this end domestic establishments are sustained to rival each other. The horses must be fine, the carriages as large and cumbrous as possible, the servants as showy in their livery as anybody's . . . not because each person takes pleasure in the display, but because everybody else does the same thing."[1]

Describing the aloofness of women office workers who detest the condescension of "patronizing society" women and the idea of being classed as workers, Mrs. Woodward explains it in these words: "They live by the standards of the whole western world, which looks down on them because they work for a living. If they were women of education working for a living, this condescension would be less. If they were

[1] Peel, Mrs. C. S., *A Hundred Wonderful Years*, p. 94, Dodd, Mead & Company, New York.

women of wealth working for fun, it would not exist at all. So naturally they pretend to both education and wealth."[1]

The manner in which profit-seeking producers capitalize on this weakness in human nature is aptly revealed by Mrs. Woodward, whose experience in selling has been varied. There are two kinds of cosmetics concerns. There are those who sell one or two brands of cold creams and powders through drug and department stores in large volume at low price. The others "operate in an atmosphere of elegance and illusion which enables them to charge fantastic prices—to add from 500 to 1,000 per cent to their costs."[2]

These latter observations show how subtly the operation of conspicuous consumption merges with that of emulation. The latter is so important in attempting to explain the origin of human choice that Chapter 9 is devoted to its consideration.

Summary

It is the argument of this chapter that throughout the realm of economic life vast amounts of goods and services are wanted by individuals not alone for the direct utility which they may yield but as means to another end. Human vanity is served by a pompous display of power in a pecuniary society which measures success on a monetary basis. A conspicuous, wasteful consumption of wealth is a convenient means of demonstrating individual power. Any theory of value which ignores this motivating force back of demand is defective.

QUESTIONS FOR DISCUSSION

1. Why do you suppose so many domestic servants are dressed in uniform?
2. Do you think a stenographer should be permitted to dress as well as her employer's wife?
3. Should manual workers be permitted to own automobiles?
4. Where does real purpose end and display begin in the use of dinner service?
5. What are your table manners? What difference does it make how you eat?
6. To what extent do you dress to excel?
7. Which sports are best adapted to conspicuous display?
8. If you were able to make a substantial gift to your college would you do it anonymously?
9. Do you think the desire for display is universal?
10. How does the tendency of consumers to choose goods for display fit into the accepted theory of demand?

[1] Woodward, Helen, *Through Many Windows*, p. 148, Harper & Brothers, New York, 1926. [2] *Ibid.*, p. 304.

PROBLEMS AND PROJECTS

1. Analyze your consuming standards critically; to what extent do you buy goods and services to show off?

2. Describe the consuming practices of the most conspicuous consumer on your campus; in your city.

3. To what extent are fraternity and sorority dances on your campus used for conspicuous display? To what extent is membership in such organizations motivated by a similar desire?

4. If you attend a private college inquire into the reasons lying back of its name and the names of various buildings. What proportion of its endowment was provided by anonymous givers?

5. Go into that section of your city in which persons with European backgrounds live, and secure illustrations of conspicuous consumption such as elaborate weddings, christenings, or funerals.

8

Fashion-Made Wants

The Power of Fashion

The Power of Fashion Is Beyond All Reason. In their more rational moments consumers may laugh at the vagaries of fashion, but unless they conform to fashionable methods of consuming they themselves will be laughed at. Unless they wish to be dubbed as queer it is as important for consumers to choose goods which are in fashion as it is to conform to the dictates of custom. In fact, fashion is a significant phase of custom. The power of fashion is so great that it compels consumers to act in quite the opposite manner from economic men. Decisions to purchase commodities in fashion reflect group power over the individual rather than a rational, original choice.

Failure to conform to fashion may lead to more serious results than mere discomfiture. It may affect one's economic status as well as one's social position. If the fashion among men is to wear the hair closely cropped, violation of the fashion by a young man may lead his superiors to conclude that he is careless or queer. Such a conclusion may very easily be a basis for the more important decision not to recommend him for promotion. Overalls may be fashionable on the farm, in the factory, or at hard-times dances, but they are distinctly unfashionable in a classroom, courtroom, or church. A beautiful Oriental costume may be admired on the stage and tolerated at a costume ball, but at other places such queer clothing is taboo for an Occidental, and that taboo is usually respected. Fashions change from time to time and differ from place to place. The old adage that when in Rome one should do as the Romans do is still an important guide to conduct for consumers. Substitute New York or Chicago for Rome, and the suggestion that consumers follow the fashions explains the origin of a significant portion of consumer demand.

The Ancient Power of Fashion. The force of fashion in determining consumer choice is by no means of modern origin. The recorded history of mankind is filled with accounts of slaves to fashion. Women painted their faces and penciled their eyebrows six thousand years ago very much as they have in recent years. "We shall wear furs in any month we are told to and go as nearly naked as the laws will permit" for the

sake of fashion. "We shall in the main go without, or put on, in and out of season, in divers shapes and innumerable quantities, such perfectly new and correct things as are presented to us."[1]

In the medieval period men were the tools of fashion. It was King Edward III who told the English people how to dress in the middle half of the fourteenth century. A new style for men and women came in early in his reign, which dates from 1325 to 1377. Another change in fashion occurred about 1350 and prevailed until 1380. The next change in English dress did not occur until 1422 and lasted until 1467. These changes in fashion were introduced at comparatively long intervals as compared with modern practice. Yet a contemporary writer complained that

> "No form of apparel liketh us longer than the first garment is in the wearing, if it continues so long. . . . Such is our imitability that today there is none like to the Spanish guise, tomorrow the French toys are most fine and delectable. And, as these fashions are diverse, so likewise it is a world to see the costliness, the curiosity, the excess and the vanity, the pomp and the bravery, the change and the variety, and finally the fickleness and the folly that is in all degrees."[2]

The power and extremity of fashion were even stronger in France. Gabrielle d'Estrées, mistress of Henry IV, "was so loaded with gold, silver and precious stones that it was absolutely impossible for her to move about at all in full dress, and almost impossible for her to stand up. . . . "[1]

In the period dominated by Marie Antoinette, fashions in women's headdress reached previously unattained extremes. "The scaffolding of gauze, flowers, and feathers was raised to such a height that no carriages could be found lofty enough for ladies' use. The occupants were obliged either to put their heads out of the windows or to kneel on the carriage floor so as to protect the fragile structures."[1] In the two years from 1784 to 1786 French fashions in women's hats changed seventeen times.[1]

These scattered illustrations and the abundant evidence which is available on the history of fashion seem ample to justify the conclusion that "Fashion seems always to be making new demands on her slaves and they seem ready to obey her mandates no matter to what they may lead.[3] . . .[3] Fashion knows no limitations, no spiritual, esthetic or material obstacles; it recognizes only man's susceptibilities and his weak-

[1] From *The Psychology of Dress* (pp. 348, 156, 209, 211), by Frank A. Parsons, copyright, 1920, by Doubleday, Doran & Company, Inc. [2] Baldwin, Frances Elizabeth, *Sumptuary Legislation and Personal Regulation in England*, p. 194.

[3] From *The Psychology of Dress* (pp. 300, 326), by Frank A. Parsons, copyright, 1920, by Doubleday, Doran & Company, Inc.

nesses and it is bound only to satisfy them, whatever or wherever their demands."[1]

What Is Fashion?

Fashion and Style Contrasted. The word style is derived from the Latin *stilus*, an instrument used in writing on waxed tablets. From the narrower meaning of anything resembling the ancient style the modern word carries the connotation of any distinctive or characteristic mode, expression, presentation, construction, or execution in some field of art. Fashion, on the other hand, is the prevailing style at any given time. Because of its changing nature it has also been defined as "a series of recurring changes in the choices of a group of people which, though they may be accompanied by utility, are not determined by it."[2] Mode is merely a synonym for fashion, while a fad is a miniature fashion in some unimportant matter. Fads are usually associated with novelties, yet many things which come in as fads may become fashions and carry over for several seasons. A style as a characteristic or distinctive method of expression is permanent. It continues as a style even though it may be out of fashion. Thus styles under Edward III, Louis XIV, or those of 1905 are still distinctive methods of expression. It is not uncommon for styles to go through a cycle of fashionability. During one period it may be fashionable for women to wear long skirts, followed by a fashion of short skirts, in turn followed by a recurrence of long skirts.

Custom has been defined as a long-established group practice or usage. The distinctions between custom, style, and fashion may be illustrated in the case of clothing. In the United States it is customary to wear clothing. Clothing styles, as a characteristic method of expression, are vastly different from clothing styles in some other countries. This is to say that there is a distinctive American style of dress, yet this style is subject to frequently recurring changes which are described as fashions.

Fashions are not necessarily progressive. They may introduce new styles or they may simply reintroduce old styles with very little or no relation to utility. They may be described as progressive or retrogressive according to the extent to which they promote human welfare. It may be fashionable for women to wear fur neckpieces in the summer and to expose their necks to wintry blasts, but in neither of these cases does the fashion contribute to their welfare.

Taste is the power to discern and appreciate that which is beautiful and appropriate. Nystrom thinks a style may be artistic, but if it is not

[1] See footnote 3 on page 113.

[2] Kitson, Harry D., *The Mind of the Buyer*, p. 68, by permission of The Macmillan Company, publishers. Essentially the same definition is given by Ada H. Bigg in her article "What Is Fashion," in *The Nineteenth Century*, vol. 33, pp. 235–248.

in fashion good taste forbids its use. Conversely, goods in style may be ugly, but good taste adapts them in an effort to secure a beautiful effect. This leads to the conclusion that "good taste is essentially making the most artistic use of current fashions."[1]

Fields of Fashion

Dress. Probably the outstanding area of consumption in which fashion prevails is in dress. The influence of style and fashion in clothing are probably as old as the custom of wearing clothing. "Verily people are always the same, with the same impulses, the same vanities, the same hypocrisies, and the same absurdities. The medieval woman fared no better and probably did no worse than her sister of today. Individual manifestations in costume were a little different, that is all."[2]

Philip Stubbs, in his *Anatomie of Abuses*, deplored extravagance, waste, and imitation in dress. He was particularly annoyed by the fashion which permitted the lowest classes to "go daiely in silks, velvettes, satens, damaskes, taffeties and suche like; not withstanding that they be bothe base by birthe, meane by estate, and servile by callyng."[3]

Certainly modern fashion finds its chief expression in the realm of dress, although modern advertising is doing all in its power to encourage adoption of new fashions in an ever-increasing range of commodities. This is particularly true for women's costumes, whether in America, or western Europe, or proletarian Russia. A prominent designer of women's clothes was invited by Soviet officials to give a fashion show for Russian women. She reported a keen interest in clothing fashions. While a majority of the Russian women had permanent waves and tinted fingernails, very few of them were wearing hats, but 80 per cent wore berets.

Annual edicts of New York and Parisian *couturières* determine for millions of women whether skirts shall be long or short, high- or low-waisted, tight- or loose-fitting, wool, silk, taffeta, or cotton. If Dame Fashion requires that women's hair shall be long or short, straight or wavy, that heels shall be high or low, that shoes shall be white or black or colored to match the costume, that fingernails shall be long or short, colored or uncolored, that eyebrows shall be plucked or penciled, her millions of followers will obey implicitly. If she demands that hats shall be made of straw or wool to resemble the Austrian Tirolean style they will be so made and fashionable; if she decrees that winter coats must be trimmed with fox fur and that women must carry a muff to match there will be no hesitancy in obeying; if she orders her followers to expose their

[1] Nystrom, Paul H., *Economics of Fashion*, p. 7, The Ronald Press Company, New York, 1928.

[2] From *The Psychology of Dress* (p. 42), by Frank A. Parsons, copyright, 1920, by Doubleday, Doran & Company, Inc.

[3] Baldwin, *op. cit.*, p. 186.

backs in the ballroom and on the beach or to wear anklets in winter and full-length hose in summer, a demand for such fashionable styles is created. So powerful and restless is the force of fashion that, in contrast to the generation or more of life that styles formerly enjoyed, the average life of the modern style is two years. Six months of that time are required for its introduction; the fashion then enjoys six months of vogue, and one year of diminishing popularity.[1]

While men at one time were mirrors of fashion they are much less susceptible to its modern force than women. This is to say that men are more closely bound by custom in choosing wearing apparel. Indeed, the power of custom is so strong that for most men a change of style in clothing is rare. This is not nearly so true as it was a generation ago. If modern merchandisers have their way the next generation of men will be as susceptible as women to the power of fashion.

It was not so very long ago that custom required men to wear heavy woolen clothing the year round. Many are still bound by the custom of wearing hats. Generally speaking, however, modern men have adapted their clothing more largely with an eye to comfort and utility than to fashion. Minor concessions are tolerated in the width of trousers or the cut of a coat, but no important recurring changes are permitted. In the opinion of two consumer engineers men are not yet fashion-conscious although they are becoming increasingly clothes-conscious. " . . . it is impossible for any man to escape style today. . . . Every day in every way the circle of fashion draws closer about him. . . . Manufacturers, retailers, and advertising may someday get together and set themselves with determination to the task of promoting co-ordinated fashion changes in masculine apparel."[2] If and when that day comes, men's freedom of choice will be still more restricted. An idealized picture of the ultimate in fashionable dress for men of the future, if tailors have their say, was contained in a display of men's clothing on Fifth Avenue. The exhibit included twenty-nine complete outfits, including field hunting costumes with red cutaway evening coats for hunt balls to be worn with black evening suit trousers. The fashionably dressed man of the future may wear club coats with monograms and sports attire which harmonizes with women's garments.

Fashion in Houses and House Furnishings. Consumer engineers are making tremendous effort to widen the field of commodities subject to fashion changes. It is their belief that modern products must be styled according to the new American tempo. Their use must convey more than

[1] Allen, Leon, "Fashion, Advertising, and the Press Agent," in *Printers' Ink*, vol. 121, p. 25.

[2] Sheldon and Arens, *Consumer Engineering*, pp. 119, 123, Harper & Brothers, New York.

mere utility. To be a fashionable user of a fashionable product it must stamp one "as in the know, as up to date, as being aware of what is being done."[1]

To the consumer engineer, fashion is not art but acceptance. Only those styles which are actually being used and bought are in fashion. Outside the realm of wearing apparel acceptance and purchase by five million families is necessary to the existence of a fashion.[2]

Architectural styles in houses come and go with sufficient regularity to classify them as fashions. Whether the architecture of a house shall be Colonial, English, Spanish, Mexican, Italian, or one of many other possible styles depends upon the period in which it is built. Home builders do not have complete freedom of choice if they have respect for fashion. Even a man of wealth would be ridiculed if he were to build a house of mid-Victorian style in the middle of the twentieth century.

Furniture and furnishings of a house also reflect the influence of fashion. Furniture for the living room will be mission style, overstuffed, leather, cane, or steel, according to the influence prevailing in the period when it is purchased. The influence of Louis XIV returns periodically to determine furnishings of bedrooms, while that of Queen Anne determines the type of silver service used in the dining room. Styles in dishes range from gold and silver to china and cut glass. One can tell with a high degree of accuracy when one's hosts were married by the style of their house furnishings.

Formerly kitchens and bathrooms were more or less private precincts in which the power of fashion was unknown, but in recent years these rooms have shown the brilliance of color required by fashion. The fashionable housewife must have a two-tone colored kitchen equipped with the latest designs in gas stove, refrigeration, electric toaster, ironer, cabinet, and sink. The crowning touch in fashionable furnishings is the brilliant red alarm clock which merrily rings in the new fashion of each new day.

Other Fields of Fashion. When automobile engineers designed their first cars they were concerned primarily with performance. Appearance was a matter of accident rather than design. It did not take consumer engineers long to discover that even if women did not buy family cars their influence was strong enough to turn the sale to the one which caught their eye by its fancy color, luxurious upholstering, and numerous gewgaws. Results are reflected in modern automobiles and in methods of selling where a large part of salesmanship emphasis is placed on style.

[1] CALKINS, Earnest Elmo, "The New Consumer Engineer and the Artist," p. 115, in FREDERICK, J. George, *A Philosophy of Production*, The Business Bourse, New York, 1930.
[2] SHELDON and ARENS, *op. cit.*, pp. 106, 107.

The automobile industry was one of the first to adopt the policy known as obsoletism. Each year new models are produced whose difference, if any, is chiefly in appearance. The fashionable consumer, "the one who is in the know," buys a new car each year, absorbing a 30 to 40 per cent loss in depreciation to prove that he is "aware of what is being done." Consumer engineers contend that this is desirable because the usefulness of anything is dependent upon our attitude toward it. If it makes us feel ashamed or uncomfortable or if it depresses us we will hate it and try to replace it, "for we human beings not only use things . . . we also use up styles."[1] Whether consumers use up styles or not and regardless of whether the idea is their own or that of profit-seeking producers, the tendency is none the less wasteful. The philosophy of obsoletism is the logical conclusion of a profit economy. It is a tendency which ought to be curbed rather than cultivated. An economic system organized to produce goods for use would have little room for obsoletism. Yet the power of fashion in selling automobiles was strong enough to compel Dodge Brothers and Ford to add fashion to utility. Fashion in automobiles, as in clothing, has reached the point where preferences in color vary by state, and from month to month. It is necessary for color experts to study fashion trends in anticipating changes in demand. At one time, whereas 40 per cent of the drivers in New England selected black cars, only 16 per cent of Southwestern motorists chose that color. Blues and grays were their favorites, followed by greens.[2]

While the power of custom is far more important in selecting foods, nevertheless fads and fashions are not uncommon. A discovery like that of vitamins is popularized by pseudo-scientists so that it becomes fashionable.[3] Raisins, breakfast foods, and confections follow the fashion cycle. Even beverages have their day and cocktails are a novelty.

In plays and movies public choice is influenced by passing events and through the theater language is rendered susceptible to fad and fashion. Games and sports do not escape. Golf, once disdained as a game for old men, and tennis, likewise regarded as a game for ladies, are now fashionable. College football is fashionable and professional football is not, while professional baseball is fashionable and college baseball is not. Cricket is fashionable in England, baseball in Japan, and volley ball in Turkey. This is not to say that these games do not have other utility, but merely emphasizes the influence of fashion in determining what games shall be played and where. It is quite possible that in another generation games which are now fashionable will be replaced by others.

[1] SHELDON and ARENS, *Consumer Engineering*, pp. 62, 63, Harper & Brothers, New York.
[2] *Automobile Facts*, February, 1939, p. 3.
[3] "Vitamins Go To War," in *Business Week*, July 10, 1943, pp. 57–69.

Basically, human love of luxury and of conspicuous and competitive consumption call for constantly changing styles so that leaders in the field of consumption may have new claims to leadership and superiority.

Democracy. Among specific conditions essential to the spread of fashion is a spirit of democracy. In a caste country there can be no sweep of fashion. In addition to restrictions of purchasing power among the masses there are restrictions attaching to social position. Even though consumers might be able to buy fashionable products their lowly status operates as a bar. In some cases this is fortified by legislation prohibiting the use of certain commodities by those outside the ranks of nobility. In those countries where the idea of political equality prevails there is a desire for economic equality. Even though it cannot be attained it can be simulated by the use of fashionable goods.

A Wide Diffusion of Income. Where a democratic spirit prevails and there are consequently no artificial restrictions on the power of consumers to purchase what they wish, there may still remain the restriction of limited purchasing power when income is so unequally distributed that only a fortunate few can buy fashionable products and their use cannot spread rapidly or far. On the other hand, if there is a fairly wide diffusion of income and a productive ability to manufacture effective cheap imitations of fashionable goods their market will be widely extended. The economic system of the United States probably comes nearer to meeting these requirements than that of any other country. This is not to imply that all citizens enjoy a higher standard of living than in other countries, but is merely a recognition of the fact that a larger proportion of the citizens possess enough purchasing power to enable them to buy large quantities of fashionable products or cheap imitations of them. The American system of large-scale production has created an economic machine capable of supplying large quantities of fashionable goods or imitations at low prices.

Transportation and Communication. Effective means of transportation and communication facilitate the spread of fashions. These agencies include rail, highway, and air transportation, and such means of communication as moving pictures, radio, and newspapers. Here also the United States is more fortunate than other countries of wide expanse such as Russia, China, and India. As recently as a generation ago the slow spread of fashions from New York westward was a favorite source of jokes. But where it was formerly a matter of weeks or months before new fashions reached the hinterland, modern means of communication have greatly reduced the time required for the spread of a new idea.

Advertising. Supplementing the spontaneous spread of fashions through the normal process of communication is the influence of advertising. Deliberately planning to secure widespread consumption of fashionable goods, and spending hundreds of millions of dollars for the use of effective means of communication, modern merchandisers are able to carry on what they call national advertising campaigns for the purpose of recruiting purchasers of their products. Human desire to follow the group, to be up to date, is effectively capitalized. That advertisers make effective use of fashion is shown by the testimony of one of their own number in whose words "much of it [fashion] is buncombe, and buncombe must be used in part in promoting it." The writer of this line concludes that it is silly to use "reason why" advertising to influence a woman to wear a fur in July or sheer silk hose in December; if the advertisement simply says it is the style she will wear them.[1]

Leisure. An increasing amount of leisure time in which to display and use new fashions is essential to their continuance. Obviously if women have to spend all their time in the kitchen there is no opportunity to display the latest acquisition in gown, wrap, or hat. Among people of the middle class, women are the most faithful followers of fashion. Perhaps this is true because men in that group are so busily occupied in making a living that they have little leisure except in the evening. It is Veblen's idea that these men, wishing to consume conspicuously and being unable to do it themselves, expect their women to do it for them. Consequently luncheon bridges and afternoon teas afford convenient opportunities for displaying the latest acquisitions in fashions.

The importance of leisure is emphasized at resorts and playgrounds, where the influence of fashion is probably strongest. At the more exclusive resorts the self-acknowledged elite of society initiate and propagate the newest styles, which are rapidly and faithfully imitated by various income groups wherever they may be found, struggling to make an impression by consuming conspicuously and frequently beyond their means.

A Philosophy of Change. Fashions thrive best in a group characterized by a liberal, in contrast to a conservative, philosophy of life. By liberal philosophy is here meant a philosophy which accepts change unhesitatingly and without question. It is obvious that if a group is dominated by the belief that what has been or what is constitutes the ultimate in desirability there will be little opportunity for a new style in consuming to gain acceptance. Curiously enough, probably one of the strongest allies of fashion is war. Under pressure of accepting new ideas the group

[1] Smith, W. K., "The Mystery in Style Creation," in *Printers' Ink*, vol. 121, No. 4, p. 25.

mind grows accustomed to change. It is in such an atmosphere that fashion flourishes freely.

Factors Retarding New Fashions

In addition to the negative aspects of the preceding factors favoring fashion, and to the factors favoring custom, the three following influences must be mentioned as opposing the force of fashion.

Inertia and Dislike for Change. It seems to be characteristically human that once a method of consumption is adopted the tendency to continue in customary channels is one of the strongest obstacles to the spread of fashion. In their consuming activities most people dislike change. This practically amounts to saying that the forces of habit and custom are more powerful than the force of fashion. It is a curious fact that men, who in the productive aspect of their lives are of necessity little influenced by custom, are much more rigidly bound by customary consumption than women. In the matter of dress particularly they are much less susceptible to changes of fashion. Perhaps this may be explained in part by the very nature of their occupation. Engaged as they are throughout the day in a business struggle where nothing is certain and change is common, they may relish the stability of customary consumption which it is their privilege to enjoy. On the other hand, women who spend their days in an unchanging kitchen find its drab monotony so wearing on their nerves that they seek relief in the excitement of change. It is this, perhaps, more than anything else which renders women peculiarly susceptible to the power of fashion.

Religion and Secret Societies. Religion, secret societies, and lodges tend to retard the spread of fashion not only because they are handmaidens of custom but also because they are guardians of group morals. Since some new fashions are commonly regarded as immoral their adoption may be actively opposed by members of religious and secret society groups. If Dame Fashion decrees that women shall smoke she is likely to find powerful opposition in these quarters. If she decrees that women may wear shorts for summer comfort she may find again the realm of her authority blocked by these organizations. Even so mild a decree as one permitting men to appear coatless at summer functions will usually result in a demonstration of the superior power of these retarding forces.

Sumptuary Laws. Attempts to regulate consuming activities of large numbers of people by legislation merely reflect the force of group custom and morals. Such legislation is comparatively rare in the United States, particularly the type which would interfere with fashion. From medieval times down to comparatively recent days English consumers have been told by Parliament what they might consume in the way of

food and clothing, to such a degree as to affect considerably the adoption and spread of new styles. Perhaps the most obvious illustrations of sumptuary regulations in the United States are those concerning indecent exposure. The force of custom, strong as it is, which requires men and women to be properly clothed in public is in most communities supplemented by a law or an ordinance providing penalty for violation. In recent years nudists have caused great concern in some communities, resulting in police action to combat this new fashion. More common and probably more significant are the regulations at beach resorts concerning the types of bathing costumes permitted. In most cases such regulations are aimed at the so-called "daring" beach costumes.

Who Starts Fashions?

Can Producers Control Fashion? There are those who believe that producers deliberately start and stop fashions. On the surface there is much which appears to support such a view, but a moment's reflection will reveal its falsity. Such an idea implies that producers have complete control over consumer demand. If such a condition prevailed it might well be described as a businessman's paradise. With confident assurance producers would then be able to direct their attention to the production of such goods as would yield maximum profit, so timing changes in styles as to maintain a continuous market for their products.

Even in such circumstances the fundamental conflict of interests among producers seeking their own self-interest would result in competition to secure control over fashion which would lead inevitably to losses for some. A swing in fashion from long skirts to short would cause losses to producers of materials used, while a change in fashion from leather to cloth shoes would yield a profit to manufacturers of shoe cloth at the expense of leather manufacturers.

As fashion is stronger than individual consumers it is also stronger than individual producers. In fact, there is some evidence that it is even stronger than groups of producers. In the long run producers organized to manufacture on a large scale in anticipation of demand stand to lose more than they gain by capricious changes in fashion. Lacking effective control over consumer demand, producers of fashion goods incur considerable risk in manufacturing new style commodities for which no want is assured. Huge investments may be made in equipment and materials necessary to produce a new-style shoe, dress, or hat. If consumer demand has been incorrectly anticipated stocks of goods can be sold only at a loss. A few years ago a department store in Philadelphia stocked heavily on men's green velour hats, manufactured to sell at $10 each. Men of that city were not attracted by the innovation in color,

with the result that the entire stock could be cleared only by offering the hats for sale at $1 each. Nystrom gives many illustrations of futile efforts of producers to control fashion.[1] One of the most elaborate attempts was made by woolen, cotton, and silk manufacturers in 1912 to offset the trend toward tighter skirts. Their objective was to secure adoption of a pannier skirt which required at least 50 per cent more fabric. Co-operation of Parisian dressmakers was secured. The new styles were exhibited at fashion shows and attractively described in numerous magazine articles. Co-operation of department stores was secured, particularly in providing attractive window displays. Huge amounts of money were spent on the campaign, but to no avail. The fashionable trend toward narrower skirts was stronger than producers. It was also stronger than individual consumers who did not dare fly in the face of fashion.

Can Advertisers Control Fashion? If producers could not compel women to wear full skirts and women could not resist the fashionable trend toward tighter skirts, who may we say was responsible for the change? Can advertisers mold consumer demand where mere merchandisers fail? Is there in fact a possibility of creating demand? "Creative Advertising" is the suggestive title of a well-known advertising text which implies that advertisers can create consumer demand. There are many in the advertising fraternity who believe in the power of their art to influence consumers. Mr. W. K. Smith, an advertising manager for a lace concern whose business dwindled when silk underwear was adopted, wrote strongly about the power of advertising to force styles on consumers. Yet the editor of *Printers' Ink*, in a note on Mr. Smith's article, suggested that the author had better inform himself of the numerous failures of such attempts.[2]

While Nystrom denies the power of advertisers to control fashions and gives illustrations to support his view, it is his contention that what advertising can do, and does, is to spread the acceptance of goods already in fashion. This, of course, is quite a different function. It is a new version of the old practice of climbing on the band wagon once the crowd has been attracted. In Nystrom's judgment advertisers are prone to claim much more credit than the facts justify. It is questionable if advertising or sales promotion has ever seriously altered any fashion trend. Fashions go out in spite of all efforts to hold them, and new ones spring up without conscious calling forth. There is much luck involved in advertising fashion goods which "take." "The heroes of business, the Napoleons of finance, the captains of industry, and the big business men of the world who are

[1] Nystrom, *op. cit.*, chap. I.

[2] Smith, W. K., "Can the American Manufacturer Force Styles?" in *Printers' Ink*, vol. 121, pp. 10–12.

the objects of much popular worship are, more often than not, merely lucky in riding in with the tide of great fashion movements."[1]

Do Consumers Set Fashions? At some point in the fashion cycle there must of necessity be some individual or group with sufficient authority to determine positively whether a fashion will be accepted. Spontaneous though the system may be, control does lie somewhere. In the final analysis it will be found that this control rests with consumers collectively. This is not to say that producers either individually or in groups do not exert considerable influence, nor to deny that individual consumers in many cases sway powerfully the trend of fashion. What it does mean is that producers suggest new fashions in their various fields but authority to accept or reject rests with consumers collectively. Once a new-fashioned product is offered on the market its fate is beyond the control of the producer; it lies wholly in the laps of consumers. If it strikes their fancy they accept it and the producer reaps profits. If it arouses mild curiosity it will enjoy a short and incomplete vogue. If for some reason it does not please consumer fancy it will be flatly rejected. It is estimated that each year in peacetime there are 200,000 dress models shown at the Paris openings. Out of that number not more than 200 can be expected to find acceptance in the United States, and of the 200 accepted here perhaps 20 will be copied in all price ranges to become a fashion.[2]

Which Consumers Set Fashions? The voice of royalty was at one time final in the realm of fashion. Whatever kings and queens adopted, even by accident, became fashionable. While Louis XIV was on a hunt accompanied by one of his mistresses, the Duchess de Fontanges, a gust of wind blew aside her elaborate headdress. She removed one of her garters to tie her headdress in place, allowing the ribboned ends to fall over her forehead. King Louis was so delighted with this innovation that the entire court adopted the fashion and it even spread to England.[3]

The influence of King Edward III in England has already been mentioned. In the reign of King Henry VII, his mother, Margaret, Countess of Richmond, established herself as supreme arbiter of fashionable mourning attire. The lower the rank, the shorter and narrower the tippet, and the less fur one might wear. Correct attire varied after the first, second, and third months of mourning and so on throughout the period.[4]

In the realm of fashionable clothing for women the influence of royalty has waned, but that of Paris is still strong. " . . . Paris still has supreme control of fashion's trend" for "Louis XIV may rightly be

[1] Nystrom, Paul H., *Economics of Fashion*, p. 16, The Ronald Press Company, New York.
[2] Sheldon and Arens, *op. cit.*, p. 127.
[3] Parsons, *op. cit.*, p. 164.
[4] Baldwin, *op. cit.*, p. 124.

said to have made and unmade France, and France the civilized world, so far as matters of art and fashion are concerned."[1]

Long ago England assumed control over conservative male fashion in clothing. Influence of royalty over men's clothing has never approached the extent of royal influence over women's fashions. This is not to say, however, that royalty does not have some authority. So popular a member of the British royal family as the Duke of Windsor was criticized by London hat manufacturers when, as the Prince of Wales, he appeared to have joined the hatless brigade. Eager to remedy that serious error, the Prince immediately ordered a half dozen gray toppers and the next day was widely photographed in his new headdress.[2] Although not all the men of England rushed to buy gray hats, the Prince's influence was sufficient to have the force of edict for many who had no more serious things to occupy their attention.

The influence of royalty in the United States is quite naturally less than in Europe. May it be said then that it is the wealthy people of this country who set fashions? Those who lack royal blood but are none the less emperors of wealth? In a pecuniary society placing such emphasis upon vast accumulations of wealth as a measure of success it would be surprising indeed if the authority of the successful did not reach beyond their own circle. Where the advertiser of a European fashion seeks to encourage its adoption by securing the endorsement of a countess or a duchess, an American advertiser may seek the same end by securing the endorsement of a famous woman of great wealth; or he may get the same favor from a President's wife, or a stage or screen star, or some other person conspicuous to the eyes of the masses.

The modern follower of fashion is not so much moved to action by what an isolated individual of royal blood or great wealth displays as by the proportion of people regarded as smart who are wearing the latest creation. One woman wearing beach pajamas can scarcely start a fashion, but if most of the socially elite adopt such an innovation it stands a fair chance of wide acceptance. Thus Nystrom concludes that

> "To find the earliest indications of new fashions and fashion trends one must find groups of people who have wealth, at least enough to make it possible for them to buy freely beyond the boundaries of absolute necessities, leisure in which to plan for and make use of fashion goods, freedom from dominating restraint of custom or habit, courage to try new things, intelligence, shrewd

[1] From *The Psychology of Dress* (p. 320), by Frank A. Parsons, copyright, 1920, by Doubleday, Doran & Company, Inc. During the occupation of France in World War II the fashion center shifted to New York.

[2] *New York Times*, July 17, 1935.

appreciation of the social significance of the events and affairs of the world, good taste with a real basis in artistic sense and, last but not least, a keen desire to compete with other people for pre-eminence in style and fashion."[1]

Why Do Fashions Change?

The Puzzling Cycle of Fashion. Perhaps the most puzzling thing about fashion is the rapid and increasing rate of change. In the time of King Edward III fashions lasted for many years, but in modern times their average span is about two years. Considering only fashion changes in clothing, can they be explained as a search for beauty and perfection? Miss Bliss thinks that man dresses and changes styles in his twofold effort to rehabilitate himself with all he lost in evolution to the human level and to attain the "absolute freedom, comfort, suitability and beauty of attire displayed elsewhere in nature." In consequence he is displeased with ill-fitting, unsuitable, unlovely garments, and each generation strives for the perfect human costume. Since this is only approximated he is constantly following an elusive goal. Thus back of every important style change is a change in mental outlook.[2]

It is significant to observe that children are rarely if ever concerned with fashion. Not until humans reach the period of adolescence are they particularly concerned with personal appearance. This leads Miss Bliss to suggest that sex is another factor explaining fashion changes. In animal life decorative features reach their height at puberty. This is the means which Mother Nature uses to draw the sexes together for reproduction. A carry-over of this influence causes humans subconsciously to decorate themselves.[2] These explanations imply that national groups have not achieved and will not achieve beauty and perfection in style. They also suggest that the quest for perfection will lead progressively toward greater beauty. It requires little observation to find numerous national costumes which, judged by any common standard, are fitting and beautiful. In many cases these costumes continue without change for generations. On the other hand, in a country so under the influence of fashion as the United States new innovations frequently mark a definite step backward rather than forward in the quest for beauty and perfection. Some modern fashions may be considered much less beautiful than former ones. Indeed a survey of fashions over a period of years reveals some which are positively ugly. Finally it must be observed that not all fashion changes bring in new styles. It is not at all uncommon for the styles of a preceding generation to be revived.

[1] Nystrom, Paul H., *Economics of Fashion*, pp. 33, 34, The Ronald Press Company, New York. [2] Bliss, Sylvia H., "The Significance of Clothes," in *American Journal of Psychology*, vol. 27, pp. 217–226.

Fashions and Conspicuous Consumption. Veblen, in his rather extreme analysis of fashionable dress, attributes changing styles to their value in proving the wearer's freedom from the necessity of working. It is his contention that the standard of reputability in a pecuniary society requires that all dress should show wasteful expenditure. Yet an effort to explain changing fashions as a means of consuming waste is insufficient, for it is purely negative. Like Miss Bliss, Veblen accepts the idea that "changing styles are an expression of a restless search for something that will commend itself to our esthetic sense." This suggests that we shall ultimately attain perfection. Indeed, Europeans and Orientals have evolved national costumes which are usually more beautiful and less wasteful than American costumes. This is to be explained by the fact that those people are relatively homogeneous, stable, and immobile. For them competition in conspicuous leisure has taken the place of competition in conspicuous consumption. This leads to the conclusion that "fashions are less stable and least becoming in those communities where the principle of a conspicuous waste of goods asserts itself most imperatively."[1]

Veblen then contributes the following explanation of fashion changes. Although a pecuniary society requires conspicuous wastefulness in clothing styles, sheer wastefulness is abhorrent even to exponents of the doctrine of conspicuous waste. To overcome this inherent abhorrence each innovation in style simulates some ostensible purpose, but the simulation is so transparent that the natural abhorrence of waste soon causes a spirit of rebellion which seeks satisfaction in a still newer style. The latter, however, to be acceptable in a pecuniary society must also be wasteful. It is not long, therefore, before followers of fashion seek refuge in another change. "Hence, the essential ugliness and unceasing change of fashionable attire."[1]

Do Women Dress to Please Men? Can fashion changes be explained as the attempt of members of each sex to win favor of the opposite sex? To a certain degree it may be asserted that women dress to please men. To a less degree it is probably true that some men dress so as to attract women. But while sexual appeal may explain decorative dress it fails to explain changes. In the animal world the male is usually more brilliantly plumed but his decorations are the same from year to year. If this were the explanation of changing fashions it would again seem that men and women would ultimately achieve a style in dress so mutually satisfactory as to render further changes unnecessary.

Such an explanation also fails to answer the question why fashions are so prominent in women's colleges. Casual observation leads to the con-

[1] VEBLEN, Thorstein, *The Theory of the Leisure Class*, pp. 174, 176, 177. Copyright, 1912, published by The Viking Press, Inc., New York.

clusion that women dress as much to arouse envy among their sisters as to please men. Why do women rebel against wearing a beautiful evening dress until it is worn out? The only apparent answer to such questions is that there is a large element of conspicuous consumption in fashionable attire.

Fashion As an Adjunct of Conspicuous Consumption. This leads to the explanation that fashion is a result of competitive display to demonstrate individual or group superiority. Both Miss Bigg and Professor Kitson find the psychological basis of fashion in imitative reverence and competitive imitation. "Fashion is just the outcome of an ignoble desire to flaunt real or simulated superiority in the eyes of the world." Competitive imitation is the desire to assert equality with the one imitated. The motive back of such imitation may be hunger for companionship on the part of those who know they must conform to group practices if they expect to be included.[1] Those who are imitated seek to differentiate themselves. This they cannot do by sumptuary laws. Consequently when their imitators become too numerous their style is no longer distinctive and it becomes necessary to change in order to maintain their position. This leads to constantly changing fashions. Eventually, originality of fashion leaders plays out and they find it necessary to revive old, discarded styles.

Fashion As an Outlet. Mrs. Woodward, whose practical merchandising experience lends authority to her view, is so impressed with the power of fashion that in her judgment "with the American buyer you have to put over a fashion first; once that is done price does not matter." She regards the restless desire for change in clothing styles as a healthy outlet. It is perfectly normal for humans to want something new or different. In her judgment a change is the most beneficial medicine in the world for people who are fatigued or bored with life as they find it. For those who cannot change their entire lives or occupations Mrs. Woodward thinks that even a new line in dress may offer relief.[2] This sounds very much like Hobson's explanation of why men drink intoxicating liquor. Perhaps it is more than a mere coincidence that in general men are less bound by fashion but are addicted to liquor as a means of escape, while women, who are much less prone to indulge in intoxicants, find their outlet in the thrill and excitement attendant upon fashion changes.

Very similar is Nystrom's explanation that fashion is a result of fatigue and boredom with life, or of curiosity and a rebellious opposition to convention. People of considerable wealth who have no real life interests

[1] KITSON, *op. cit.*, and BIGG, *op. cit.*, on page 114 of this book.

[2] WOODWARD, Mrs. Helen, *Through Many Windows*, pp. 328–345, Harper & Brothers, New York.

easily become completely engrossed in themselves, their dress, and their surroundings. Lacking a philosophy of utility they become victims of a philosophy of wastefulness. Restlessly they seek excitement and satisfaction in change. Fatigued and bored with the commonplace they find momentary thrill and satisfaction in the acquisition of new clothing cut on different lines. The same explanation may be applied to any objects subject to changing fashions.

Other Explanations. An explanation applicable only in the temperate zones is that which links fashion change to seasonal changes. The closing point of any fashion is a change in season. When winter ends, the fashions of that season pass into history. By the time the next winter season arrives new fashions are in vogue. So it is with each of the four major seasons. Most people welcome the advent of a new season and mark the event by a rather complete change in clothing. Thus arrival of spring is characterized by a change to spring clothing. Summer in turn brings out its distinctive apparel, while fall and winter provide additional opportunities for changing costumes. In some localities this applies also to other objects of consumption. For example, it is customary for some households to take down and put away curtains and draperies in summer. While these changes in season require compensating changes in consuming habits, there is no fundamental reason why the same articles of dress and other goods might not be used for several years in the proper season, but some think nothing is older than last year's fashion, and hardly anything could cause more embarrassment to a woman or a man than to be compelled to wear clothing out of fashion.

Curiosity plays some part in explaining fashion, particularly among those whose interests in life are shallow. Curiosity leads to a desire for new sensations. There are women, for instance, for whom there is no greater flattery than the remark that they seem always to appear in a dazzling new gown. Whether it is true or not is unimportant. It pleases them and encourages them to try to live up to such a reputation.

There are always a few rebellious spirits in any group. The power of custom is after all stronger than that of fashion. The static tendency is stronger than the dynamic. This being so, there are frequently a daring few who rebel against the rigors of custom. This they may do in a number of different ways, but one effective means is to flout customary styles in clothing. There are those who enjoy the sensational publicity attendant on their appearance in public in new attire which thoroughly shocks most members of the group. From time to time as these rebellious moods break out, new styles are inadvertently perpetrated on the public to be picked up and followed by the more courageous of the imitators.[1]

[1] NYSTROM, *op. cit.*, chap. 3.

A Synthetic Explanation of Fashion. Each of these several explanations of fashion contributes something toward understanding this peculiar phenomenon. Yet no one of them alone seems adequate. Perhaps if the main points of all these ideas are drawn together we may more nearly approach an understanding of this important factor affecting consumer choice.

In the case of clothing, where the power of fashion is strongest, the biological sex appeal explains desire for decorative dress. Perfect beauty and harmony are sought but not attained. A small wealthy group with much leisure time and no real interests in life seek relief from boredom or attempt to satisfy their curiosity by indulging in the momentary thrill of a new costume. Lacking any other means of demonstrating superiority, they attempt to set themselves apart by a conspicuous display of wearing apparel. The imitative tendency of those in lower-income groups leads them to emulate the new styles. This deprives leaders of their distinction, forcing them in self-defense to discard old styles and adopt new ones. Pressure of imitators so taxes the originality of fashion leaders that they are sometimes compelled to revert to former styles. New styles may be useful, but the essence of fashion is waste. This restless change revolves about seasons and perhaps explains the greater prevalence and faster tempo of fashion in temperate zones.

Fashionable Waste

The Wastefulness of Fashion. The very essence of fashion is wastefulness and obsolescence. As a consumer one can seldom be both fashionable and economical. There is little room for fashion in the concept of the economic man. By their very nature fashion goods sell, temporarily, at monopoly or semi-monopoly prices. Genuine competition is alien to fashionable goods.[1]

The available evidence goes to show that fashionable goods sell at fashionable rather than ordinary prices. This is partially explained by the fact that fashion is such an important adjunct to conspicuous consumption. In buying a new-fashioned sports frock for $19 the customer may get really $4 worth of dress and $15 worth of fashion; and if so, from a purely economic point of view the $15 would represent sheer waste.

Fashion and Obsolescence. Obsoletism is a word coined by the new fraternity of consumer engineers. In their own words it "is another device for stimulating consumption." Clothing, motor cars, bathrooms, radios, refrigerators, and furniture go out of style and are replaced long before they are worn out. People are persuaded to abandon the old and buy

[1] For an interesting example of monopoly prices for fashion goods, see Sheldon and Arens, *Consumer Engineering*, p. 113.

the new so they may be up to date. Consumer engineers contend that there is no waste in this process. The statement that "Wearing things out does not produce prosperity, but buying things does"[1] shows clearly the profit-seeking viewpoint of modern businessmen. They hold that consumers must be made to buy; if new commodities are not needed then an artificial desire must be created; if the present automobile is capable of giving several years of satisfactory transportation service the owner must be made so dissatisfied with its old style that he will junk a perfectly useful piece of wealth. This may create prosperity for producers but certainly not for consumers. The principle of obsoletism is nothing more than the consumer engineer's version of the make-work fallacy. It is predicated upon the assumption that if consumers did not junk useful wealth and buy fashion goods they would do nothing else with their purchasing power. If they really knew their own self-interest they would use their limited incomes to buy other genuinely useful goods and services. While this would detract from the prosperity of producers of fashion goods, it would increase the prosperity of other producers and result in a net social gain.

Whom Do Fashions Benefit? The only possible gainers from the artificial stimulation of fashion are a few specialists producing fashion goods. Large-scale producers manufacturing in anticipation of demand stand to lose as a result of capricious changes in fashion. These losses must of necessity be anticipated and an allowance made for them. As a consequence fashionable goods cost more. Thousands of dollars may be spent in producing a new-fashioned commodity only to find that consumers disdain it. The immediate loss falls on the producer, but the ultimate loss falls on consumers and society in general. Contrary to the popular belief that fashion is the lifeblood of trade, it actually increases hazards and uncertainties in economic life. Those fluctuations in business activity which are called business cycles reflect the restless philosophy of fashion. Reduction rather than encouragement of fashion in consumption would go far toward stabilizing economic life.

Do Fashions Contribute to Human Welfare? Consumer engineers contend that consumers buy style as well as goods. In the present state of organization this is probably true, but to admit the truth of such an assertion is not to admit that such a practice promotes human welfare. This and previous chapters have presented evidence which goes to show that consumers frequently act so as to retard rather than promote their own welfare. Motives back of fashion are snobbish and ulterior. Such satisfaction as some people derive does not justify the social cost of fashion.

[1] Calkins, Earnest Elmo, in Sheldon and Arens, *Consumer Engineering*, p. 7, Harper & Brothers, New York.

This is not to condemn desirable changes but rather to question the genuine utility of artificial values artificially created. Those who seek to set themselves apart by attaining pre-eminence in fashionable consumption could secure the same or greater distinction by engaging in constructive creative activity. The result would be greater social gain in the form of genuine human welfare. Consumption would be directed toward utility rather than waste.

SUMMARY

Throughout the centuries, fashion, defined as the prevailing style in consumption, has operated as a powerful and formidable influence on consumers. Fashion is not necessarily progressive. It predominates in those fields of consumer choice affecting dress, houses, house furnishings, automobiles, and sports. Among factors favoring fashion are a spirit of democracy, a wide diffusion of income, effective means of transportation and communication, advertising, an increasing amount of leisure time, and a philosophy of change. Forces opposing fashion include inertia, religion, secret societies, and sumptuary laws.

Producers are powerless to determine fashion trends. Advertisers can help to spread new fashions but are unable to initiate or stop them. Producers may suggest new fashions but in the final analysis it is consumers who exercise control. Some consumers are more important than others as arbiters of fashion. Royalty once enjoyed more power over fashion than at present. In the United States both wealthy persons possessed of leisure and freedom from customary restraints, and other persons of prominence, with courage, intelligence, good taste, and a competitive spirit, are leaders of fashion.

Increasing shortness of fashion cycles is difficult to explain. Some seek to explain fashion changes as a sex phenomenon; others as an imitation of natural life. Some find the explanation in the desire to consume conspicuously. Fashion is regarded by some as a means of escape from drab routine, while others associate it with seasonal changes. A composite or synthetic explanation of fashions in dress recognizes the sex factor and the restless search for beauty and harmony; it includes curiosity, efforts to escape boredom, imitativeness, and the seasonal factor.

Fashion is responsible for tremendous waste. A fashionable person cannot be an economic man. The only possible gainers from fashion changes are a few specialists engaged in producing fashion goods. Consumers as a group suffer economic loss, as do many producers. Fashions do not contribute to genuine human welfare; they actually interfere with its advancement. The wise consumer will substitute rationality for blind adherence to fashionable decree.

QUESTIONS FOR DISCUSSION

1. If you dress according to latest fashion, although the costume may be unbecoming to you, are you dressed in good taste?
2. To what extent is your choice of clothing determined by fashion? What about your choice of hats? Your choice of books to read?
3. To what extent are your parents influenced by fashion in choosing a house? House furnishings? Automobile?
4. Do you agree with consumer engineers that we not only use up things but also use up styles?
5. Is the philosophy of obsoletism valid?
6. Are you enough happier in having the latest fashion in clothing or automobiles to justify discarding items not yet worn out?
7. In Chapter 2 it was suggested that there is a caste system in the United States. If true what is its effect on fashion?
8. According to the National Resources Committee, how was national income distributed in 1935–1936? How would that distribution affect fashions in the United States?
9. Can you give an illustration of a producer's attempt to start or stop a fashion?
10. Who starts fashions on your campus? Compare your answer with that in the text.
11. Are those whom President F. D. Roosevelt called "economic royalists" the ones who start fashions in the United States?
12. What economic purpose does fashion serve?
13. Who gains and who loses as a result of fashion? Viewed broadly, do you think the gains are greater or less than the losses?
14. In your study of principles of economics did you find fashion included as a factor affecting consumer demand?

PROBLEMS AND PROJECTS

1. On the basis of observation on your campus do you think women or men are the greater slaves of fashion? Is custom or fashion the stronger force at your college?

2. List clothing fashions now prevalent on your campus; compare them with fashions two years ago; compare them with fashions ten years ago, as revealed in your college yearbook.

3. As you visit the homes of several friends notice the type of furniture. Can you place the approximate time of purchase by its design?

4. Choose five current fashions and seek to explain how they started on your campus.

5. Question 25 or 50 women on your campus or on a city street; ask them to what extent they dress to please men and to what extent they seek to excel or emulate other women.

6. Review Nystrom, Paul H., *Economics of Fashion*, or Veblen, Thorstein, *The Theory of the Leisure Class.*

9

Imitative Wants

Why Do Men Work?

To Acquire Wealth. The usual explanation of why men work is that by working they get wealth with which in turn they hope to satisfy their wants. Each man is supposed to contribute according to his ability and to be rewarded by the same standard. The lowly and incapable may be able barely to meet subsistence needs, while others, more fortunate in their talents, work hard to secure additional income with which to satisfy their desire for comforts and luxuries. If the wage or profit which a man receives for his work is less than he can get in some other occupation he will not hesitate to change positions even though it means moving to a new locality. This economic explanation of why men work is thus simple, definite, and measurable.

Other Reasons: Desire to Create. In fact the above answer to the question is too simple for reality. It either ignores or underrates the importance of several other motives. One of these is the universal human desire to create something. So common and so powerful is this tendency that in the judgment of many writers it is inborn and instinctive. The instinct of workmanship, as Veblen has shown, characterizes all productive effort from the most intelligent worker to the least intelligent. From childhood on, men enjoy the peculiar satisfaction attendant on the feeling of having created something useful. For this reason purposeless work is degrading for most men. Nothing will more quickly break a worker's morale than realization that the work he is doing is futile. Experience in providing jobs for men on work relief supplies ample verification. If men were concerned only with the income received it would make no difference what kind of work they were asked to do.

The instinct of workmanship also may help to explain why men of means continue to work long after they have secured an accumulation of wealth whose income will enable them to live as luxuriously as they wish. Having been occupied for years in building up an enterprise, the rich man has no more wish to desert it than to desert his own child. Such men have the feeling of having created something and of wanting to nurture it to full maturity, so they continue to work regardless of the size of their income.

Desire for Prestige and Power. Another human tendency so universal and strong as to be classed by many writers as instinctive is the desire to rise above the level of the group in exercise of power and in securing recognition. In a primitive, nonpecuniary group this instinctive urge for prestige and power finds expression in exploits requiring physical strength and skill. Leaders in such a group who enjoy recognition and authority are those whose exploits command respect. Ambitious ones attempt to emulate their achievements, while the more slowly are satisfied to pay homage.

As a pecuniary society developed, in which success is measured by monetary standards, acquisition of wealth became the one dominant means of securing prestige and power. Wealth thus becomes not an end in itself but a means to another end. Instead of being used only for the direct satisfaction which it may yield, it is acquired and used also for the indirect satisfaction of demonstrating pre-eminence over the group. This helps to explain why men of great wealth continue to acquire more. Although they may possess more wealth than they can possibly consume they continue to struggle for still more. It is not enough to be counted among the ten wealthiest men of the country; ultimate satisfaction can be achieved only by having more wealth than any other person.

With this development in the importance of wealth as a means to an end, the method of acquiring it loses significance. In the judgment of those seeking pre-eminence the matter of how one attains his wealth is not nearly so important as the amount of wealth he can acquire. Thus predatory activities gradually become less harshly judged by members of the group. If one can secure great wealth as a result of rendering great service it is fortunate, but if the road to riches can be traveled more rapidly by engaging in unsocial activities there is a powerful tendency to travel that way. Once a man secures a fortune the group is less likely to ask by what means it was obtained than to inquire how large it is. This so changes the standards by which success is achieved and measured that physical weaklings endowed with shrewd acquisitive powers may become financial giants and leaders in a purely acquisitive society. Just as primitive men were compelled to demonstrate their physical skill and prowess so that all might see and be convinced, so modern men feel compelled to demonstrate their financial power. A huge accumulation of wealth can have utility as a symbol of acquisitive strength only if all members of the group are aware of its ownership. A man possessed of a modest fortune enjoys no prestige as such if others in his group are unaware of his holdings. Only by consuming conspicuously can the owner prove his claim to power and prestige. Thus lavish expenditure becomes a means to an end.

It may be noted parenthetically that the development of this idea by Veblen led him to conclude that since wealth is merely a symbol there can never be too much of it. Economists have long contended that it was impossible to produce too much wealth, since man's wants are capable of indefinite expansion. But Veblen's idea goes farther and proceeds along different lines to explain why the stock of wealth can never be sufficient. It also comes closer to reality in a society in which wealth is so unevenly divided. Even though the amount of wealth in the United States should be doubled, tripled, or quadrupled there would still be severe competition among those already very wealthy to determine who could secure the largest portion of it.

Pervasiveness of These Forces. Any impression that acquisitive, competitive, emulative instincts are characteristic only of those who have won group recognition must be corrected. These tendencies are universally inborn. They may be stronger in some individuals than in others, but the economic organization in which we live nurtures them in all persons. The chief difference between those who have and those who do not have wealth is not in their attitude toward it but in their ability to acquire it. Obviously all members of the group cannot be the most wealthy, but if they cannot be first they may strive to be second; if they cannot be within the first ten they may struggle to be within the first hundred. If they cannot be in that select group whose annual incomes are $100,000 or more they may attempt to place themselves among those who have $50,000 or more. Going on down the scale, those who are unable to be in the higher-income brackets make every possible effort so to increase their earnings as to place themselves in the $10,000-, $5,000-, or $3,000-income group. While they cannot equal those at the top they can at least excel those at the bottom. If a man can rise from the $3,000- to the $5,000-income group he may realize as much satisfaction as a modern Croesus would derive by moving from the $3,000,000- to the $5,000,000-income class. Throughout all income groups the desire to equal those at the top or to excel those below becomes a pressing incentive to win coveted power and prestige. This desire and tendency powerfully affect the economic activities of most men and color the choices of many consumers. Purchase of commodities becomes a means of demonstrating financial power. Many things are wanted for what they will yield in prestige rather than for any inherent power directly to satisfy the purchaser's wants. "With the exception of the instinct of self-preservation, the propensity for emulation is probably the strongest and most alert and persistent of the economic motives proper."[1]

[1] Veblen, Thorstein, *The Theory of the Leisure Class*, p. 110. Copyright, 1912, published by The Viking Press, Inc., New York.

Emulation in Consuming Wealth. It has already been suggested that in its broader sense emulation is that human characteristic which causes individuals to wish to excel or to equal others in some field of human activity. The word itself carries no connotation of desirability or undesirability. Church members may seek to equal or excel others in Christian living, while gangsters may seek to equal or excel the exploits of a Capone or a Dillinger. The term is used here with special reference to consuming activities. Emulative consumption is a by-product of conspicuous and fashionable consumption. Although the fundamental purpose of producing goods is to enable consumers to satisfy human wants and enrich human living, the human tendency to emulate has caused consumption to be regarded by many as a means of invidious comparison. As a result wealth is endowed with a secondary utility as evidence of ability to pay. The more expensive a commodity the more utility in the secondary sense it possesses.[1] To the extent that emulation guides consumer choice the difference in its effect upon individuals is largely one of degree. The same motives guide the consuming activities of the small-town banker's wife as those which regulate consuming standards for the wife of the nation's richest banker.

IMITATIVE CONSUMPTION

Emphasizes Use of Obvious Goods. Emulative or imitative consumption thus becomes competitive consumption. Competition in buying assumes new significance. Instead of rivalry among buyers to purchase at the lowest price it becomes a rivalry in which buyers compete with one another to prove their financial superiority by the character and volume of their purchases. This causes the economic buyer who haggles over price to lose social caste. Only those who buy on a grand scale, and to whom price is no consideration, are able to maintain the desired social position.

The popular conception of competitive consumption is expressed in the phrase "keeping up with the Joneses." Human experience is filled with comedy and semitragedy in attempts to keep up with one's neighbors. An amazingly large percentage of limited family incomes is spent to bolster up family pride. While the breadwinner struggles to equal or excel Mr. Jones in the size of his pay check, his wife struggles with equal determination to equal or excel Mrs. Jones in the grandeur of her expenditures.

This competition has a strong tendency toward extravagance in

[1] VEBLEN, Thorstein, *op. cit.*, p. 154.

using goods and services whose consumption is much in evidence, while the rest of consuming life is likely to be shabby. " . . . The worst failures in any community are oftener those of families who have made every effort to live like their much richer neighbors than of families who have disregarded public opinion in matters (other than morals) that affect social standing."[1]

Clothing, for Example. Since clothing is much in evidence it becomes an effective means of demonstrating family ability to keep up with the pace set by others. It is often said that in American life one must dress according to one's position. It is fitting and proper that manual workers should wear rough, heavy clothing designed for comfort and durability, but it is considered altogether improper for white-collar workers, whose incomes are as likely as not to be less than those of manual laborers, to wear clothing which marks their economic status. The office boy and bookkeeper must emulate the junior executive, who in turn imitates the dress of his immediate superior. The stenographer must wear silk hose and a fur coat to demonstrate her ability to dress as well as the more highly paid women employees. This practice forms the basis of the common complaint that one cannot distinguish, by the clothing worn, between the office boy and the boss's son, nor between the stenographer and the boss's daughter. Such satisfaction as the office boy and stenographer realize is frequently purchased at the expense of nourishing food or adequate shelter. If income will not permit the purchase of real silk hose and dresses, a cheaper imitation such as rayon or artificial silk will be used. Thus the millions of consumers in lower-income groups constitute a large market for cheap imitation merchandise. Such commodities are bought not for their inherent utility but for such ability as they may possess to give the wearer a little more prestige. If he cannot excel or equal others he must secure such satisfaction as is possible by imitating them.

Parties. While this competitive consumption in clothing is a common practice in business life, it attains full significance in that phase of social intercourse which we call society. Throughout all economic classes the propensity for parties provides abundant opportunity for competitive consumption. Clothing styles for men are practically on a noncompetitive basis. Customary formal dress is so standardized that the only possible difference between an evening suit of a millionaire and that of an unemployed office worker is in the quality of the material used. But among women there is not a trace of such standardization. In fact the tendency is increasingly in the opposite direction. True, women are

[1] Lord, Isabel E., *Getting Your Money's Worth*, p. 125, Harcourt, Brace and Company, New York, 1922.

regulated to some extent by fashion, but they pay dearly for it. Expenditures for feminine evening gowns may range from a comparatively few dollars to thousands of dollars for an individual garment with supplementary jewels and fur wraps. Those who have ability to pay have ample opportunity to demonstrate it. In every social group, whether it be metropolitan or rural, there must of necessity be one or a few women who dominate competitive consumption. They are the leaders who set the pace which others struggle valiantly to maintain. The inability of imitators to keep up is a confession of their leader's superiority and a confession of their own weakness. Chagrin and humiliation are partly tempered by the satisfying knowledge that still other women in the group cannot come so near to equaling the standard of competitive consumption.

A large number of American men are so busily engaged in struggling to increase their money incomes that they have comparatively little time to indulge in competitive consumption. That is to say, there has not yet developed in so new a country a very large group of second- or third-generation heirs with sufficient competence to relieve them of all economic responsibility. This situation throws an added burden upon women as consumers. The wife of a typical successful American businessman is his social front window. By dressing her up and showing her off he is able to demonstrate, to all who see, his ability to provide not only expensive clothing but leisure time. The latter of course implies that there are household servants. According to competitive practice the standard of high reputability requires that a woman must have not only expensive clothing but considerable variety. It is a serious reflection upon the businessman if his wife is compelled to wear the same evening gown more than once. Further down the income scale the same standard prevails, but necessity requires that a gown be worn an entire season or more. A college instructor at one time resigned his position to go into business, expecting to earn enough money so that his wife would not have to wear the same evening dress four years in succession. In Booth Tarkington's *Alice Adams* the father gave up his good position and jeopardized his honor to start a glue factory of his own for the sole purpose of making enough money to secure for his daughter entree to the social life of the town.

By their parties many people are judged. In each group lavishness of entertainment at luncheons, teas, dinners, dances, and week-end parties settles toward a minimum standard which all must attain to retain membership in that social circle. The competitive process tends constantly to raise the standard, resulting in the impoverishment of those near the lower margin. It may even result in forcing them to fall into

the social life of the next group below. Even among wives of college professors, where one might expect to find a larger degree of rationality in consumption, similar competitive standards prevail. Those receiving higher salaries set a pace which makes it extremely difficult for those further down the scale. Even compacts are difficult to carry out. In one such group competitive consumption in dinner bridge parties became so intolerable that the men attempted a truce under which expenditures for dinner and prizes were to be limited. The first part of the agreement simply failed to work, and the problem was solved by eliminating dinners. Efforts to set a price limit on prizes were only partially successful. No one of the sixteen families in the group was willing to accept the implication that it could not afford to give as expensive awards as the Joneses. The failure of this plan in such a group makes it easier to estimate the power of competitive consumption in determining choices of consumers in general.

Houses. The locality and the house in which a family live provide additional effective means of demonstrating pecuniary power. Nearly all villages and cities have their slums and their swanky sections. Leaders in each group usually will occupy the best house on the choicest street, while competitors will place themselves in as favorable a location as circumstances permit. If a family cannot afford a house on Fifth Avenue or the North Shore they can at least bask in the sunshine of reflected glory a block or two away. If a suburban dwelling is the smart thing a family must make every effort to locate in or near the choicest suburb. This is essential, for by their location they know they will be judged. Even department stores grant credit on the basis of one's address.

But address alone is not sufficient. The family home must be up to the standard of its location. If it has a $20,000 address it must be a $20,000 home, and so on up or down the scale. On this basis every town and city is zoned. A keen observer could estimate with a high degree of accuracy the annual income of any family on the basis of its address.

The growth of apartment-house living has operated partially to destroy the accuracy of an address as a guide to the occupants' pecuniary power. While distinction attaches to apartment-house addresses, they are not so effective as the addresses of one-family houses. The modern cliff dwellers who live in apartments lead semidetached home lives which demonstrate their social position to neighbors ineffectively. Such obvious things as expensive automobiles or summer vacations at fashionable resorts assume added significance, so that one's competitive consuming power is marked by the name of his car and his forwarding address.

House Furnishings. When a family entertains competing members of its social group its social position is still further determined by the

elaborateness of house furnishings. The latest and most expensive types of furniture, rugs, dishes, silver, books, and pictures yield in addition to direct utility the peculiar satisfaction of demonstrating financial ability to own the newest and the best. Owners of Oriental rugs may enjoy their beauty and soft pliability, with their suggestion of luxury, but the final pride of ownership is derived from the friendly envy of those as yet unable to compete. Solid silver may be no more serviceable or beautiful than plated silverware, but satisfaction is enhanced by the admiring expression of guests who furtively discover the sterling mark.

Among intellectuals a personal library has long been accepted as a mark of culture. This standard has been widely imitated as a part of standard home equipment by persons lacking the capacity to enjoy good books. Mrs. Woodward, describing her early selling experience, says, "Our books were gaudy and expensively made. . . . The people who bought . . . sets were trying to buy with money some certainty about their intellectual standing; they had a clutching desire to be exclusive; they were snobs to whom the limited number of impressions in an edition and the high price gave some social satisfaction." On one occasion 3,000 sets of Shakespeare, full of glaring errors in spelling, with folios upside down or completely missing, were sold, yet not a single complaint was received. A large order was placed with a wealthy woman who wanted the binding to match the color scheme in her library. What the books contained was immaterial. In some cases such buyers of books actually purchase false backs to fill numerous shelves in their libraries.[1]

Country Clubs. Membership in exclusive clubs, lodges, and even churches is another means by which competitive consumers imitate their superiors in an effort to prove their ability to maintain the approved consuming standard of their group. Public knowledge that one is a member of an exclusive, which means expensive, organization yields rich returns in indirect satisfaction. To be able to entertain lavishly in one's home is public evidence that one is on the ladder leading to social success, but to be able to entertain in an exclusive country club is evidence that the host is one rung further up the ladder. A new standard is thus set which imitators may copy.

Keeping Up Appearances on Credit

Living Beyond One's Income. If family income does not permit purchases on a scale sufficient to keep up with the pace set by leaders in the social group, the use of credit offers a convenient means of maintaining status. In contrast with a cash sale in which the exchange of a commodity

[1] Woodward, Mrs. Helen, *Through Many Windows*, pp. 74, 84, Harper & Brothers, New York, 1926.

for cash is simultaneous, a credit sale involves the exchange of merchandise for a promise to pay at some time in the future. Supplementary to the use of credit is the return privilege, particularly common among urban department stores. Credit managers of such firms are all too familiar with cases of women customers who purchase goods on credit with the return privilege, returning a hat, dress, or coat after wearing it once or twice. It is difficult to detect such practices, and credit managers must be very careful not to offend customers. As a result there are some consumers who find it possible to keep up with the Joneses at the expense of other people.

The tremendous expansion of installment buying in the 1920's and 1930's, reaching a peak in 1940, made it possible for millions of consumers to keep up appearances by spending their anticipated income. As long as the consumer has an income to anticipate he may continue indefinitely to spend it in advance. To be sure he may pay dearly for the privilege of purchasing goods before he can pay for them, but if he is obsessed with the idea of imitating the consuming standards of more fortunate competitors he may find the temporary satisfaction sufficiently great. If the time comes when income is curtailed or stops entirely those who have deluded themselves into thinking that they could maintain indefinitely a scale of living beyond their income are subjected to a rude awakening.

Installment selling and buying has become such an important institution in American economic life that an entire later chapter—Chapter 14—is necessary to consider adequately all its implications for modern consumers.

Inconspicuous Economy

Saving on the Unseen. Since the very essence of competitive imitation in consuming is spending more than one's income justifies on things which all the world can see, it follows that there must be a compensating economy in the use of things that are not conspicuously used. This is merely an extension of the common practice of letting children wear stockings whose visible portions are perfectly sound but whose toes and heels are broken through. The financial strain of keeping up appearances may compel economy in the type and quality of underwear, bedding, mattresses, and similar articles which are usually invisible; but even in such cases an exception is made for a guest room, where all the furnishings, including mattress and bedding, must be such as to create the desired impression. Throughout the household there are numerous opportunities to skimp and save on items which are less commonly noticed. One of the most common sources of humorous remarks by

children is the practice of serving elaborate party food for guests in contrast to the meager daily diet, of which no one outside the family knows. And have you heard of a working girl who eliminates breakfast and lunches on chocolate malted milk so that she may save enough to pay the installments due on her fur coat? She is not entirely a creature of fiction.

Equally common and perhaps still more serious is the practice of driving an automobile without insurance protection. There are millions of cars on the highways whose owners cannot afford garage rent or insurance premiums. Not only is the car something which yields direct satisfaction, but it is also visible proof that its owner has enough income to imitate the consuming standard in his group. Insurance protection for the lives and property of others is intangible and invisible. It does not readily serve the purpose of proving ability to pay. In consequence many survivors of the thousands of men killed in fatal automobile accidents each year are deprived of economic livelihood because the drivers of death-dealing cars had spent their limited incomes on things more visible than insurance premiums. The time is rapidly approaching when consumers in general will insist, as they have in Massachusetts and Ohio, that no one can afford to own or drive an automobile who cannot afford insurance premiums for provision of payment of damages in case of deaths or injuries caused by his car.

Similar in nature and seriousness is the practice of competitive consumers in spending so much of their income on things which others can see that there is little or nothing left for the purchase of insurance protection for dependents in case of accident, illness, or premature death. In contrast to the philosophy which leads men to attempt to provide for future contingencies, imitative consumers are exponents, unconsciously perhaps, of the philosophy expressed in the saying "Eat, drink, and be merry, for tomorrow we may die." In the face of limited income very few consumers can have both economic security and a sufficient surplus to spend in attempting to keep up with others whose income is larger or who are making no provision for their future security. In an economic system which grants to consumers freedom of choice in setting consuming standards the only remedy for over-emphasis on visible goods which bring immediate satisfaction lies with consumers themselves. This amounts to the same thing as saying that as long as consumers have freedom of choice they will continue to act as they do. Here again perhaps consumers as a group will sometime require a more adequate system of social insurance to which competitive consumers will be required to contribute, since their unprovided-for dependents would otherwise become a charge on society.

Custom. Attention may be called briefly to the fact that custom is the negative aspect of emulation. As the chapters on customary consumption have shown, consumers are guided to a large extent by custom. Custom determines what they shall or shall not consume. Custom demands that they emulate their ancestors. This means that they must refrain from emulating contemporary violators of custom. In the consumer's mind the tendency to act customarily is constantly being combated by the tendency to imitate conspicuous and fashionable consumers. The latter course requires courage and financial power. The more income one has the easier it becomes to flout custom. Since so many people have very small incomes, most consumers are more completely under the control of custom than of the tendency to emulate. This is not to say, however, that custom predominates to the exclusion of emulation. It simply means that the emulative tendency is held in check by custom as well as by a limited income.

IS EMULATION DESIRABLE?

Does Emulation Promote Welfare? The imitative tendency in itself is neither good nor bad. It has great possibilities when used in either direction. Moral judgment of emulation depends on the forms it takes. Whom do consumers copy? And why? We must have answers to both these questions before we can determine whether emulation promotes human welfare. Possibilities for constructive, useful emulation are numerous and obvious. Emulation in good taste which leads to wider appreciation of such things as do contribute to group and individual welfare is wholly desirable. If those in lower-income groups emulate their economic superiors by developing a love for and appreciation of music, art, literature, and drama there can be no doubt that the welfare of such emulators will be advanced. If college students can be encouraged to emulate the practice of purchasing and reading good books there can be no doubt that they will benefit.

If consumers, in general, copy new ideas in types of food consumed and ways of preparing them their diet will be broadened beneficially. If they imitate desirable trends in clothing materials and styles they may gain comfort and beauty. If styles of architecture which they emulate are designed to provide comfort, convenience, and health they will benefit. If house furnishings and equipment which they copy include useful, labor-saving, health-conserving devices it is obvious that not only they but all members of the group will reap advantage. All this is well summarized by Hobson in his remark that "to copy good examples, even if the copying is defective, is an elevating practice."

On the other hand, emulation carries great possibilities for promoting illfare. If a sham aristocracy sets the consuming standard on a basis other than utility the door is opened wide for wasteful emulation. It is here that pecuniary emulation takes its greatest toll. Its whole purpose is false, with the result that falsity permeates the consuming standards of nearly all who emulate.

Summary

Men work not only for wealth with which to satisfy economic wants. They desire to create things and to acquire wealth for the prestige and power it carries. These forces operate throughout all income groups, varying only in degree. To enjoy social prestige it becomes necessary to prove one's pecuniary power by lavish expenditures, a practice imitated by others within the limits of their incomes. This leads to emphasis on such obvious consumers' goods as clothing, houses, house furnishings, automobiles, country clubs, and entertainment, at the expense of less obvious but more important goods and services. Use of credit enables some people to keep up appearances not justified by their income. All emulation is not to be condemned, for it may take desirable forms, but in the United States wasteful emulation probably predominates.

QUESTIONS FOR DISCUSSION

1. What kind of work do you expect to do? Why?
2. Have you ever observed a tendency on the part of small children to show off? Have you ever experienced such a desire? Do you ever catch yourself even now inclining to show off?
3. Can you offer any additional explanation, particularly psychological, of the tendency to show off and to emulate?
4. Do you see any connection between the distribution of national income and the phenomenon of emulation?
5. Do you agree that "the wife of a typical successful American businessman is his social front window"? Can you cite any illustrations?
6. Does your sorority or fraternity seek to excel or emulate other social groups on the campus in the elaborateness of parties? In athletics? In scholarships? Are you in sympathy with the practices of your group?
7. Have you ever abused the privilege of returning merchandise to a store? Do you know of others who have?
8. Do you know of any families who skimp on invisibles in order to make a better impression in other ways?

PROBLEMS AND PROJECTS

1. Interview ten men, asking them for what reasons, in addition to earning a living, they work. How many of them are engaged in work they enjoy?

2. Analyze your expenditures carefully; to what extent does desire to emulate others explain your economic choices?

3. Examine the influence of emulation on the choices of a selected group for clothing, housing, house furnishings, automobiles, colleges, books, and such other things as you may wish to include.

4. Draw up a list of imitative products designed for sale to emulators, such as rayon for silk.

5. Give several illustrations of desirable emulation, based on your own observation.

10

Producer-Made Wants: Advertising

Why Advertise?

It Pays. There is probably no more universal slogan than "It pays to advertise." From the time persons learn to talk in infancy until their dying day they are under the influence of advertising. It is so thoroughly and essentially a part of the American economic picture that no one can avoid it. So dominant is the philosophy of businessmen in economic thinking that their conviction that advertising pays is rarely questioned. It is curious that consumers have not more persistently inquired as to whom it pays. An English businessman, writing in 1911, thought the greatest mystery in business is why the world spends several hundred millions of dollars in advertising its productions to itself. The same writer, tracing advertising development, found that it has passed through several stages. It began as mere publicity but it quickly became combative and assertive of individual superiority over rivals. Later it adopted blandishing and seductive methods. The next stage was the dependence upon bulk, mass, and the impetus of astonishment. Finally, he wrote, in the then present stage of development (1911) misrepresentation had become the chief part of the advertiser's stock in trade.[1]

Writing thirty years later, another English businessman, while recognizing the legitimate function of advertising, holds that most competitive advertising is a costly national extravagance. "The advertising of products in the home market has little national value; it mostly results in the selling of greater numbers of unneeded articles, or in transferring business from one manufacturer to another without increasing its total volume, while the ultimate consumer, who has to pay for the advertising, gets less or inferior products for his money."[2]

If advertising pays, consumers may well ask, Whom does it pay? One certain answer over which there can be no dispute is that it pays producers. We may be sure that individual firms will not continue year after year to spend millions of dollars advertising their wares unless their

[1] Dibblee, George B., *The Laws of Supply and Demand*, p. 187, Houghton Mifflin Company, Boston, 1912.

[2] Courtauld, Samuel, "An Industrialist's Reflections on the Future Relations of Government and Industry," in *The Economic Journal*, April, 1942, p. 11, Macmillan & Co., Ltd.

profit-and-loss statements show very clearly that advertising pays them. Whether or not advertising benefits all members of society is a question which is too rarely raised and discussed. Professor Hower, in his study of an advertising agency, uses the preface to describe his own background as a frame of reference within which he approached the task of writing the history of an advertising agency. "I regarded advertising as an inevitable accompaniment of a free competitive economic system," wrote Professor Hower, "and I recognized its value to individual firms, but I was (and still am) dubious about some of its social consequences."[1]

Why Does It Pay? Just what is it that advertising does which in the judgment of hardened businessmen justifies annual expenditures of millions of dollars? If advertising pays, why does it pay? Answers to these questions have already been found in our previous discussion of consumer choice. It was there shown that consumers do not know definitely what they want. In some cases they have little idea as to what they need or desire. This is a situation created to order for advertising. Whenever and wherever consumers are at all uncertain as to what they want, there is opportunity to persuade them. Persuasion may take the form of helpful guidance and advice by interested friends. There is a great deal of this so-called word-of-mouth advertising, although there is no way of determining its exact extent or influence. The more usual form which persuasion takes is that of commercial advertising by producers who have goods to sell. They of course expect to sell their goods at a profit. If the goods are things which consumers need and ought to have, the persuasive influence of advertisers may be beneficial. But modern advertising has reached its present proportions by failing to discriminate between wealth, nealth, and illth. In fact, nealth and illth (page 52) are likely to be more extensively advertised than wealth. A publication of the American Medical Association says, "It is a truism that needs no debate that the quality of goods is in a general measure inversely proportional to the blatancy of the advertising. In the case of tooth paste, those who advertise their tooth paste as a cure for gum disease or tooth disease try to make up in false claims what their tooth paste may lack."[2] So unreal are the assumptions of capitalist economy that a poor soapmaker who advertises will do better than a good one who does not. "The chief proof of the value of advertising is that it pays a high rate of profit when extremely well done. . . . "[3] This leads to the general

[1] HOWER, Ralph M., *The History of an Advertising Agency, N. W. Ayer & Sons at Work, 1869–1939*, p. xxxi, Harvard University Press, Cambridge, Mass., 1939.

[2] *Questions and Answers on Health*, as presented by *Hygeia*, where they were originally published, pp. 33–34, The American Medical Association, Chicago, Illinois, 1938.

[3] DIBBLEE, George B., *The Laws of Supply and Demand*, p. 190, Houghton Mifflin Company, Boston.

conclusion that it pays producers to advertise whatever will yield them the greatest profit, without special regard to the ability of advertised goods to yield utility to consumers.

The illogicalness of advertising is emphasized by the words of a staunch defender of capitalism. "No sane man, if he thought the matter over quietly, would dream of buying anything on the mere assertion, by someone who wanted to sell it, that it was cheap or good." Yet this is essentially what millions of consumers are doing daily. "As things are at present, the manner in which we spend our money is a matter in which we are swayed less by intelligence than by habit and convention and sheep-like mimicry of one another, tempered by weak-minded submission to the bullying of the advertiser."[1] In fact one psychologist, a proponent of advertising, contends that consumer buying habits belong just as much to the seller as to the buyer, since they have been paid for by the money which the seller has used in advertising.[2]

The success of persuasive advertising is evidence that consumers are not sure of what they want. If they were aware of their wants they would express them in the market place in the form of effective demand. The things thus demanded would be the things which producers would then proceed to supply. But that is not what happens. With the advent of production on a large scale in anticipation of consumer demand, producers have been put under increasing pressure to force a market so as to enable them to maintain maximum output and thus reduce the cost of production per unit. Their unexpected success in directing consumer demand into those channels most profitable to themselves has resulted in the development of a major industry involving several hundred thousand workers, copy writers, layout men, printers, lithographers, and commercial artists, to say nothing of rewrite men, announcers, and high-pressure salesmen. These molders of consumer choice have found it necessary to use a minimum of fact with maximum emotion, for the average mind has little receptivity for reason. According to one advertiser, women seldom buy anything through logical reasoning, even for their babies. In the case of men it is necessary to appear to use reason but it is dangerous to be genuinely logical, for logic will not sell merchandise.[3]

Extent of Advertising

Billions for Business. The extent to which businessmen are sold on advertising can be demonstrated no better than by quoting their own

[1] Withers, Hartley, *Poverty and Waste*, pp. 124, 149, B. Smith, London, 1914.

[2] Kitson, *The Mind of the Buyer*, p. 119.

[3] Fairbanks, A. H., "Reason Why Copy and the Dear Old General Public," in *Printers' Ink*, vol. 21, p. 81. Woodward, Helen, *Through Many Windows*, p. 205.

estimates as to the amount of money spent to entice consumers to buy their particular products. As long ago as 1914 Mr. Hartley Withers estimated that the sums spent for advertising in western Europe and North America totaled $2,750,000,000 in a year. Eleven years later Mr. Edward Bok estimated that American businessmen alone spent $1,284,000,000 a year to secure access to public eye and ear. In the boom year 1929 expenditures for advertising in the United States reached an all-time high. It is estimated that at least $2,600,000,000 worth of wealth was spent that year to tell consumers what to buy.

Something of a mushroom growth was revealed by the sharp decline in advertising budgets after 1930. Some advertisers actually increased their budgets during the depression, but most businessmen found that advertising as usual simply did not pay cash returns—in spite of the ominous suggestion made in the following bit of doggerel, publicized by newspapers and magazines whose advertising receipts had shrunk:

> There was a man in our town,
>   And he was wondrous wise.
> He swore by all the gods above
>   He would not advertise.
> But one day he did break this rule;
>   And thereby hangs a tale—
> The ad was set in real small type,
>   And headed "Sheriff's Sale."

With the upswing in business activity in 1934 advertising expenditures increased as shown in Table II on page 151. The impact of war at the beginning of 1942 resulted in a decline in advertising expenditures, but, according to the *Tide* advertising index, there was a sharp increase beginning in May, 1943. In March, 1944, the index stood at 135.5 compared with 114.9 in March, 1943.

Kinds of Advertising. How do businessmen spend their millions or billions for advertising? What do they think are the most effective ways of influencing consumers? Division of advertising expenditures for 1943 provides a fairly typical answer to these questions. Of the $2,130,000,000 spent in that year $665,000,000 was spent to secure space in newspapers and $330,000,000 to reach potential buyers directly by mail. Owners of radio broadcasting stations charged $325,000,000 for sending advertisements over the air, while magazine publishers sold space valued at $225,000,000. Business and trade papers sold $75,000,000 worth of advertising. Owners of billboards lining national highways and railway tracks received as their portion $53,000,000, while publishers of farm papers sold space valued at $22,000,000. There are no data on the

TABLE II.—ESTIMATED ADVERTISING EXPENDITURES IN THE UNITED STATES, 1929–1943[1]

Year	*Amount*	*Year*	*Amount*
1929	$2,600,000,000	1937	$2,000,000,000
1930	2,400,000,000	1938	1,700,000,000
1931	2,000,000,000	1939	1,780,000,000
1932	1,500,000,000	1940	1,840,000,000
1933	1,400,000,000	1941	1,920,000,000
1934	1,600,000,000	1942	1,820,000,000
1935	1,700,000,000	1943	2,130,000,000
1936	1,900,000,000		

amount of money paid to producers of motion pictures, to theater owners for advertising on the silver screen, or to transportation companies for display cards in busses, trolley cars, and trains. Doubtless all of these and other media are included in the miscellaneous item for which $435,000,000 was spent in 1943. This division of advertising expenditures probably reflects roughly the percentages spent on each of these media each year, regardless of the total expended. It is clear that, in the judgment of advertisers, newspapers are the most important means of reaching consumers. In recent years radio has become more important, judged by advertising expenditures, than magazines in reaching consumer buyers.

This division of advertising expenditures also reveals the extent to which newspapers, magazines, and radio are subsidized by advertising. It is common knowledge that the greatest source of income to publishers of newspapers and magazines is the advertising expenditure of American businessmen. It is much less common knowledge that not only newspapers and magazines, but also direct-mail advertising are subsidized by the United States government through the granting of postage rates on second- and third-class mails which yield returns less than the cost of handling. Analysis of postal revenues for the fiscal year 1942 reveals that 52.3 cents of the postal dollar came from first-class mail, while second- and third-class mail yield 3.0 cents and 8.5 cents respectively. Normally the expenses of handling first-class mail are much less than the revenues, while the expenses of handling second- and third-class mail are much more than the revenue they yield. During the fiscal year 1942 there was a profit of $162,976,883.65 on first-class mail compared with a loss of $110,299,757.63 on second- and third-class mail. The Supreme Court

[1] These figures were secured from Mr. L. D. H. Weld, Director of Research, McCann-Erickson, Inc. Mr. Weld credits BORDEN, Neil H., *The Economic Effects of Advertising*, p. 57, for the figures 1929 to 1939; the figures for 1939–1943 are based on estimates prepared by Mr. Weld as published in *Printers' Ink*.

of the United States has held that the reason for incurring such losses year after year "was to secure to the public the benefits which result from the wide dissemination of intelligence of current events," as carried by newspapers and periodicals.[1] But at the time that policy was adopted, newspapers and periodicals were not laden with lucrative advertising as they are in the twentieth century. The real meaning of the foregoing figures is that those who use first-class mail service are paying part of the postage for publishers of newspapers and magazines and direct-by-mail advertisers. This puts them in the anomalous position of helping to pay costs of advertising which is designed to influence them to consume for the benefit of the advertisers.

One of the specific recommendations made by the authors of *Facing the Tax Problem* was that the first-class mail rate of three cents be reduced to two cents and that the revenue lost thereby be recouped in part by increasing the charges on other parts of the postal services so that the latter more nearly cover the cost of the service rendered.[2] When Congress was considering the 1942 tax bill, Representative Fitzpatrick of New York introduced a bill to increase the postal rates on second-, third-, and fourth-class mail. He estimated that the total subsidy to newspapers alone through the second-class mailing privileges had amounted to nearly a half billion dollars in the preceding five years. In writing on this bill editorially, *Printers' Ink* said that it "will probably get nowhere." So far (up till 1944), the editors of *Printers' Ink* have been correct.[3]

Far more serious in its implications, but never publicized, is the dependence of newspapers and magazines on advertisers. Even though there may be no direct conscious control of newspaper policy by advertisers, there can be no doubt that there is a vast amount of indirect and perhaps unconscious influence on it. Roger Babson fears the intensity of modern advertising and the dependency of the newspaper published upon advertising revenue. "It was never dreamed," wrote Mr. Babson in contrasting early-day advertising with that of the present, "that the income from advertising would become a factor in determining the editorial and news policies of the *news*papers."[4] The press of this country is essentially a businessman's press. Deliberately or otherwise, most newspapers see eye to eye with Chambers of Commerce on questions involving labor policy, taxation, and the proper sphere of government

[1] United States Post Office Department, *Annual Report of the Postmaster General*, fiscal year ended June 30, 1942, pp. 40, 12; *Cost Ascertainment Report, 1942*, pp. 8, 14.

[2] Shoup, Carl, Blough, Roy, and Newcomer, Mabel, *Facing the Tax Problem*, p. 435, The Twentieth Century Fund, New York, 1937.

[3] *Printers' Ink*, March 12, 1943. See also *Advertising Age*, June 29, 1942.

[4] Babson, Roger, *The Folly of Instalment Buying*, p. 243, J. B. Lippincott Company, Philadelphia. (Originally published by Frederick Stokes Company, New York, 1938.)

activity. This is not surprising, of course, since the publishing of newspapers and magazines is itself a business operated for profit. It simply serves to emphasize the dual influence of the profit motive in controlling the public press. This becomes strikingly evident whenever consumers attempt to secure legislation to protect their interests. With rare exceptions it is difficult if not impossible to secure impartial, to say nothing of favorable, publicity through a press controlled by the very interests opposed to such legislation. This point will be pursued further in the analysis of food and drug laws in Chapter 28.

Advertising Expenditures As Costs. Curiously enough, advertising expenditures are regarded as costs by businessmen but not by consumers, yet it is the consumers who pay the bills and who should regard them as costs. So regarded, it is pertinent to inquire as to what consumers get in return for huge advertising expenditures. In what ways, if any, does advertising help them to promote their own welfare? What are the specific services rendered by advertising? Unless it can be shown that the billions spent for advertising benefit consumers, Mr. Ralph Borsodi is correct in his argument that the institution of advertising merely redistributes national income without contributing anything toward enlarging it.[1]

Does Advertising Help Consumers?

Advertising Aims. In seeking an answer to the question as to whether advertising helps consumers, it must be recognized clearly that the real purpose of advertising is to benefit producers rather than consumers. While the ultimate costs of advertising may be borne by consumers, the immediate cost is borne by producers. As they constantly remind us, they are not in business for their health nor for altruistic purposes. Their one single objective is to make all possible profit. Advertising has been found a useful means of accomplishing that end. Any benefit which consumers may derive is purely incidental to the main purpose. In the following analysis of advertising this important fact must be kept constantly in the foreground.

In the following discussion distinction must also be drawn between local and national advertising. Generally speaking, the former is more likely to be helpful than the latter. National advertising is much less likely to be informative in nature, which means that it is much more likely to play upon consumers' emotions.

Consumer Benefits Claimed for Advertising

Advertising As Information. The first benefit claimed for advertising is that consumers are thereby informed where they can buy specific

[1] Borsodi, Ralph, *The Distribution Age*, D. Appleton & Co., New York, 1929.

goods or services. This is more nearly in line with the original meaning of the word, which is defined as making known by public announcement. To a busy buyer required to purchase small amounts of a wide variety of goods this type of advertising may be genuinely useful. Its helpful possibilities are limited, however, to novelty and specialty requirements, for the consumer knows that the things he needs from day to day can be found at various stores specializing in those goods. It requires no public announcement to inform consumers where they can find groceries, drugs, cosmetics, hardware, clothing, furniture, shoes, or any of the other numerous commodities they may want. Hower wonders whether it is wise to spend so much on advertising, for example, motor cars, which advertise themselves to a large extent, and on food and tobacco products, which satisfy wants that do not require stimulation.[1] There are times, however, when buyers may be uncertain as to where they can purchase less common commodities. Perhaps there is no better illustration of this type of advertising than the store directories found in a large department store.

Hower points out that advertising could be much more helpful and informative to consumers if the advertisers would "debunk" one another's sales arguments. If this were done in the proper way it could be very educational, but the borderline between fact, fancy, and disparagement is hazy. Obviously this kind of advertising would lead to more competition and probably to trouble among the advertisers. It is probably for this reason that it is considered unethical for one advertiser to attack the merchandise of another.[2]

On a commercial scale informative advertising includes business and professional announcements such as are found in newspapers, and in telephone and business directories. The lawyer's shingle and the doctor's card or name plate are enough to inform those in need of legal or medical service where it may be obtained. It is considered unethical, however, for professional practitioners to inform the public how superior they are in their professions. Other types of informative advertising include unadorned announcements of theater programs and newspaper notices of auctions, sheriff's sales, and classified advertisements announcing houses for sale or rent and personal services for hire.

Price Advertising. A second consumer service claimed for advertising is that it informs buyers of prices asked for specific goods and services. This type of advertising is frequently associated with informational announcements. Not only are buyers informed where they may buy certain goods, but the price which the seller expects to receive is

[1] HOWER, Ralph M., *The History of an Advertising Agency, N. W. Ayer & Sons at Work, 1869–1939*, p. 220.
[2] HOWER, *op. cit.*, p. 269.

included as part of the information. Newspaper and handbill advertisements, together with price placards placed conspicuously in stores, typify this type of advertising. Sales of all kinds are featured by emphasis on price. This is in contrast to the purely informational announcements used by professional men, which rarely mention fees.

To the extent that price advertising enables consumers to compare prices of competing products, and to the extent that it helps them save time in shopping, it is genuinely useful. This assumes of course that price announcements are honest and trustworthy rather than misleading. Except in the case of standardized products, comparative prices are of little significance unless accompanied by some added information concerning quality. To the extent that such information is lacking, price advertising may easily be misleading.

Advertising New Products. A third benefit claimed for advertising is that it informs consumers of new products or services that have become available in the market. Emphasis is here placed upon newness rather than availability. Of necessity such advertising must also inform consumers where the new products can be purchased. Such information is incidental to the main purpose of proclaiming a new discovery.

Modern industry is increasingly making use of research. Industrial laboratories are continually discovering, patenting, and marketing new devices for satisfying human wants. It is important to distinguish, however, between genuinely useful discoveries and simulated innovations. The automobile industry, for instance, has placed altogether too much emphasis on new contrivances and gadgets designed to attract buyers who are easily impressed with the necessity of possessing the latest model regardless of whether or not it represents a genuine improvement. According to Hower, as early as 1900 it was evident that profits to be gained from advertising were to be found fully as much in promoting the sale of particular brands of established staple commodities as in advertising new articles. "Advertising as an aid to technical progress was being over-shadowed by advertising as a competitive weapon and as a correlative of mass production." The task of an advertising agency even then was primarily not that of telling consumer buyers of new products but rather attempting to induce them to buy a particular brand.[1]

In a market comprising such a vast geographical area as the United States and composed of 136,000,000 potential consumers it would be impossible for manufacturers of newly discovered commodities to inform so many consumers without resorting to some form of advertising. Unless consumers are aware of new products they do not constitute a potential

[1] HOWER, Ralph M., *The History of an Advertising Agency, N. W. Ayer & Sons at Work, 1869–1939*, p. 116, Harvard University Press, Cambridge, Mass., 1939.

market. For generations housewives had been accustomed to preserving food in hot weather by using ice refrigerators. Discovery of the practical possibility of electric and gas refrigeration in individual homes could be made known to potential consumers only by advertising. Word-of-mouth advertising would be too slow to develop a market capable of sustaining large-scale production. Consequently the industry felt justified in spending millions of dollars to tell consumers of this new type of refrigeration.

Numerous other illustrations might be given. It was not many years ago that consumers were totally unaware of the possibility of radio. A few years before that, automobiles were unknown. In very recent times consumers have been given much information as to the possibilities of air conditioning.

The benefit derived by consumers from this type of advertising is clearly limited by the nature of the product and the amount of information provided. If the new means of satisfying wants is real wealth as we have defined it, then the service of informing consumers is useful and desirable. On the other hand, if the new device falls in the category of illth or nealth, consumers are in no way benefited by learning of it. Expensive advertising of a new whisky or a new cigarette, fields which are definitely overcrowded as well as of questionable utility, would be difficult to justify.

A telling defect in much advertising of new products is its failure really to tell consumers anything significant about it. In excited tone and glaring type consumers are told that there is a new product; they are probably told that all smart people are using it and that it is an answer to the prayer of all consumers. But there is likely to be little reliable information as to what it is, of what it is made, what it will do, and what it costs. The psychology of much of this type of advertising is to distract consumer attention from the mere matter of price to the fact of thrilling newness.

Advertising of new products is likely to be on a national scale in which magazines, newspapers, and radio are the most commonly used media for reaching prospective buyers. The combined circulations of *Collier's*, *Liberty*, *Life*, and *The Saturday Evening Post* for 1942 were approximately 11,315,000. It was estimated further that there were 58,509,000 civilian readers for these popular magazines. Examination of a typical issue of any one of these periodicals will reveal the relatively small proportion of really informational advertising in them.

Advertising New Uses for Old Products. It sometimes happens that new uses are discovered for commodities already on the market. This may come about accidentally, as a result of laboratory research or as a result of national contests in which consumers vie with one another for

cash prizes as rewards for revealing various uses which they have discovered for a particular product. Manufacturers of yeast have in recent years extolled a new use of their product as a digestive aid. Sellers of a popular brand of canned heat have conducted contests in which consumers have described a wide variety of uses for it.

To the extent that the advertisement actually increases the utility of a commodity which is real wealth, this type of advertising is helpful. The range of satisfying human wants may as readily be widened by discovering new uses for old products as by discovering entirely new goods. Such advertising would benefit producers also by resulting in increased sales of their products. It is thus possible for advertising to be mutually beneficial and economically desirable.

Actually the proportion which this type of advertising bears to the total is extremely small. It is especially common in marketing food products for which new recipes are presented. While all advertising media may be used, depending upon the type of products, such advertising is usually confined to newspapers and radio.

Making Competition Effective. A fifth advantage claimed for advertising is that it makes competition more effective. According to economic theory a consumer is protected from over-pricing and inferior quality by competitive rivalry of sellers for his custom. If one merchant charges too high a price or seeks to sell merchandise inferior to that of his competitors, buyers will turn to them. Concurrent with the decline in personal relationships in marketing, advertising has developed as a potential means of helping buyers find those merchants whose products are reliable in quality and fair in price. There can be no doubt that a large part of localized advertising accomplishes this purpose. To the extent that buyers function as economic persons they can make effective use of sales announcements by retail stores. If a grocery store advertises a special week-end-sale price on butter at 52 cents a pound while competitors attempt to maintain the regular price of 54 cents, such advertising has the tendency to compel the reduction of butter prices at all the stores to the lower level. Yet this is only a tendency, its effectiveness depending upon consumer response.

It must be recognized that much advertising is purely perfunctory, falling in the category of good-will advertising. This is especially noticeable in local advertisements. High school annuals, college newspapers and yearbooks, theater programs, and village newspapers are filled with this type of advertising. Merchants buy space not because they intend to use it for informational or price announcements, but because they hope thereby indirectly to gain the good will of a particular class of consumers. From a strictly business point of view it is doubtful whether such adver-

tising pays. It is frequently an outright subsidy which makes possible continued publication of papers and periodicals whose demise would represent no considerable loss. Cigarette smokers the country over are unwittingly paying publication costs for many college newspapers. Clearly this type of advertising has little or no effect on competition.

When advertising was in the developmental stage it was much more creative and pioneering than at present. Increasingly advertising is becoming competitive. Having established himself, an advertiser finds it necessary to defend his position in the market against new competitors offering similar goods or services. In most cases he employs advertising as one of his defensive weapons. "In giving credit to advertising as an instrument of material progress, we must remember that advertising is also used to defend established interests against change." In other words, advertising can be used to prevent competition as well as to make it more effective.[1]

Advertising can make competition keen, but it is beneficial only in so far as the goods and services advertised are beneficial. It may be argued that if consumers are determined to purchase nealth or illth, advertising which serves to maintain quality and reduce price is beneficial to them. At best this is a negative advantage.

Apparent competition is not always genuine competition. A modern holding company has proved to be a device whereby producers may simulate competition. Holding Company A may control Companies B and C, producing supposedly different brands of cigarettes. The intercorporate tie-up of these three companies is completely unknown to practically all consumers. Instead of combining the two producing companies to secure economies of large-scale production which might be passed on to consumers in the form of lower prices, Company A may continue separate operations so as to lend credence to the supposition that they are competitors. Smokers of brand B will thus continue their loyal devotion to the cigarette which suits their taste even though the price per package may be increased and the formula may be exactly the same as for brand C.

In order to encourage this illusion Company A may strengthen the supposition of competition by carrying on an elaborate advertising campaign in which the relative merits of brands B and C are emblazoned on billboards from coast to coast. In such cases advertising becomes not only a means of maintaining prices above competitive levels but becomes also a powerful means of deceiving unwary consumers.

A vast amount of advertising every year is designed to induce con-

[1] Hower, Ralph M., *The History of an Advertising Agency, N. W. Ayer & Sons at Work, 1869–1939*, p. 268, Harvard University Press, Cambridge, Mass., 1939.

sumers to pay prices in excess of competitive levels. Illustrations have already been given emphasizing this tendency. In general wholesale prices bear a close relation to costs of production. Retail prices of staple necessities are not usually far removed from producing costs, but the prices of commodities known as comforts and luxuries may be far above costs of production where they are maintained by an elaborate campaign of national advertising. "Advertised brands (of dentifrices) often sell at prices well above those of unadvertised brands of acceptable quality." Retail sales of dentifrices range from $40,000,000 to $55,000,000 a year. To sell that volume manufacturers spend $10,000,000 to $15,000,000 in advertising. This means that advertising costs average about 40 per cent of the manufacturer's selling price and 25 per cent of the price which the consumer pays.[1]

Stewart and Dewhurst give figures to show that "unadvertised goods cost less" than advertised products. For example, a standard headache remedy costs 59 cents for 100 tablets, a mark-up of 60 per cent over the wholesaler's price of 37 cents to the retailer. An unadvertised identical headache remedy is sold for 39 cents and sometimes for as little as 23 cents.[2] The average wholesale price of 12 patent (proprietary) medicines was $2.64 per ounce while for identical nonproprietary products the price was 94 cents per ounce, according to the Federal Trade Commission in 1931. "The difference of $1.70 per ounce was the price the retailer (and ultimately the consumer) paid for the advertised product."[3]

National advertisers are fond of breaking down advertising costs into minute fractions of a cent per unit of advertised products, implying that even though the consumer does pay for the advertising it really is infinitesimal. But Stewart and Dewhurst point out that although the advertising per bottle of headache remedy may be only $^{16}/_{1000}$ of a cent per bottle the cost of advertising from the consumer's point of view is much more than the direct cost of buying a page in a magazine or a half hour of radio time because, as suggested above, the buyer frequently pays more for the advertised product at retail than for unadvertised products. If as a result of advertising the consumer-buyer pays 59 cents for 100 tablets of headache remedy which can be bought unadvertised for 39 cents, then it may be said that the cost of advertising to the consumer is not $^{16}/_{1000}$ of a cent per bottle but rather 20 and $^{16}/_{1000}$ cents, since the buyer pays the unnecessary margin of 20

[1] Borden, Neil H., *The Economic Effects of Advertising*, p. 14, Richard D. Irwin, Chicago, 1942.

[2] Stewart, Paul W., and Dewhurst, J. Frederic, *Does Distribution Cost Too Much?* pp. 50–51, The Twentieth Century Fund, New York, 1939.

[3] *Ibid.*, p. 228.

cents. The 20 cents may be profit due to monopolistic competition and part of it may go to other costs of maintaining a national marketing system, but in any case the consumer pays 20 cents more.[1]

The argument that advertising is beneficial because it makes competition more effective is predicated upon the assumption that competition always promotes efficiency. This is an assumption which will not stand analysis. It is well known to those versed in economics that competition may be the death of trade as well as the life of trade. Congress and the courts have long since recognized that competition between natural monopolies of organization is wasteful. If competition itself is wasteful it follows that advertising tending to promote such competition is wasteful also. Railroad, telephone, gas, and electric companies have been given monopolistic privileges in recognition of this principle. Yet there is considerable advertising by individual firms in these industries.

The Temporary National Economic Committee found practically complete monopoly in the production of aluminum, shoe machinery, glass container machinery, optical glass, nickel, molybdenum, magnesium, and beryllium. Moreover, practically complete monopoly was found in telephone service, railroads, oil pipe lines, and operation of Pullman cars. Industries in which two firms dominated the production included domestic telegraph service (since reduced to one firm), plate glass, electric lamps, electric accounting machines, and air brakes. Monopolized markets in which a few firms control the whole supply and those in which one or a few firms control a major portion of the supply include steel, cement, agricultural implements, petroleum and gasoline, copper and lead, newsprint paper, glass containers, biscuits and crackers, typewriters, eyeglasses, cheese, radios, ethyl gasoline, automobiles, motion pictures, radio broadcasting, anthracite coal, meat, tobacco, rayon, and silk. Additional industries in which trade associations control prices thereby giving member firms monopoly power include flour, bread, household furniture, asphalt shingles, and roofing. Finally, the Committee found legalized restraint of competition in the production of bituminous coal, petroleum, trucking, agriculture, building construction, and the retail trade.[2]

In the marketing of all or most of these goods and services there is much advertising the purpose of which must be to attempt to sell more at the same or a higher price, or to sell the same amount at a higher price. Some of it may be good-will advertising. One familiar with national advertising will recognize in the foregoing lists many persistent

[1] *Ibid.*, p. 228.

[2] Temporary National Economic Committee, *Competition and Monopoly in American Industry*, Monograph No. 21, United States Government Printing Office, Washington, 1941.

advertisers. Obviously, such advertising does not promote competition. It is not helpful to consumers. Much of it is intended to strengthen the entrenched position of monopolistic firms against adverse public criticism. Economic analysis recognizes that oftentimes a monopolist may not charge the full monopoly price for fear of arousing public resentment which may result in substitution or in regulatory legislation. It seems clear that much of the advertising of these monopolists is so to strengthen their position in the public eye that they will be able to charge a price more nearly approaching the full monopoly price.

Advertising and Large-Scale Economies. A sixth advantage sometimes claimed for advertising is that it promotes large-scale production and thereby lowers prices. The argument, with its premises, runs as follows. Advertising increases sales, thereby enabling production on a large scale, yielding economies which result from large-scale organization and production. These economies which are passed on to consumers as a result of competition more than offset any increased cost due to advertising.

It will be noticed that there are several assumptions in this argument. It is presumed that advertising is responsible for increased sales. This may or may not be true. Certainly if some kinds of advertising in common use do increase sales it is an amazing reflection on human credulity. If the argument is used historically there is no way of demonstrating that advertising alone has resulted in increased sales of merchandise in general.

A second assumption is that such economies as are achieved by large firms are passed on to consumers in the form of price reductions sufficient to offset the increase in prices necessitated by advertising. A third assumption is that the costs of operating large plants are lower than for smaller ones. A final assumption is that the industry is one whose costs of production per unit diminish as production increases up to a certain point.

Facts to support or refute these four assumptions are not available. No one has ever demonstrated successfully the validity of the argument as a whole. Like the theory of the economic man it might be true if all assumptions were justified, but that in itself is an unjustified assumption. Advertisers hoped that the Harvard study on advertising would establish the validity of this argument. Some of them think it does, but the controversy continues.[1] The study shows that the demands for lettuce, sugar, green vegetables, and professional services have grown even

[1] BORDEN, Neil H., *The Economic Effects of Advertising*, especially chap. 6, Richard D. Irwin, Chicago, 1942. For evaluation of the Harvard study by advertisers see *Business Week*, January 3, 1942; *Printer's Ink*, April 3, 1942, and June 26, 1942.

though those products are scarcely advertised. The demands for cigarettes, dentrifices, oranges, refrigerators, automobiles, radios, and electric washers have been accelerated by advertising, according to the study, but not created. The efforts of advertisers to bolster the sale of cigars, smoking tobacco, furniture, wheat, flour, men's shoes, have proved futile. Borden recognizes that consumer demands are determined primarily by basic environmental conditions; " . . . advertising by itself serves not so much to increase demand for a product as to speed up the expansion of a demand that would come from favoring conditions or to retard adverse demand trends due to unfavorable conditions."[1] Does advertising tend to reduce production costs? Borden says the answer is indeterminate. There is some affirmative evidence, but it is impossible to show a clear causal relationship between decreased production costs and advertising. In fact, Borden says that "one cannot be certain to what extent the *increased* distribution costs which have attended the growth of industrialism are attributable to advertising."[2] There was some evidence that advertising had been partially responsible for building up the size of some enterprises, but accompanying evidence also showed that large size does not necessarily mean low marketing costs; on the contrary, some of the larger concerns were found to have relatively high marketing costs.[3]

Proponents of the view that advertising promotes large-scale production ignore the fact that many industries and plants producing on a large scale do not advertise at all, or advertise only on a very modest

TABLE III.—TOTAL ADVERTISING EXPENDITURES IN RELATION TO NET SALES VOLUME FOR VARIOUS MANUFACTURING GROUPS—CONSUMER PRODUCTS, 1935[4]

Product Group	*Average Percentage* *	*Product Group*	*Average Percentage* *
Proprietary Medicines	33.78%	Petroleum Products	5.68
Drugs and Toilet Articles	27.65	Sporting Goods	5.67
Soft and Carbonated Beverages	15.23	Confections, Ice Cream	5.35
Silverware, Clocks, etc.	9.31	Food and Grocery Products	5.07
Paints, Varnishes, and Removers	7.40	Clothing and Accessories	4.50
Drug Sundries	6.00	House Furnishings	4.50
Auto Accessories	5.90	Household Electrical Equipment	4.47
		Footwear	3.97

* Interquartile average.

[1] BORDEN, Neil H., *The Economic Effects of Advertising*, p. 843, Richard D. Irwin, Chicago, 1942.
[2] BORDEN, *op. cit.*, p. 851 (italics supplied).
[3] *Ibid.*, p. 853.
[4] BORDEN, Neil H., *The Economic Effects of Advertising*, p. 442, Richard D. Irwin, Chicago, 1942.

scale. On the other hand, many of the most persistent national advertisers are producers on a comparatively small scale. There is no demonstrated or apparent connection between size of the business and extent of advertising.

Advertising expenditures as a percentage of net sales range from about 4 per cent to about 34 per cent in various groups of products. The figures in detail are as shown in Table III. It is to be noted that there is a considerable range in the advertising expenditures for each group, the high point being nearly 34 per cent for proprietary medicines and closely followed by nearly 28 per cent for drugs and toilet articles. No one has thus far succeeded in proving that these additional expenditures result in lower prices to consumers. Numerous attempts have been made but the results are not fully convincing. At least equally convincing is the effort made by Mr. Ralph Borsodi to prove that advertising actually increases prices.[1] Impressive also are the figures already quoted from the careful study made by The Twentieth Century Fund. It is at least as fair an assumption as any other that if the greater part of advertising budgets in many industries were applied to direct price reductions consumers would probably gain.

It is quite possible for a firm to grow so large that it becomes uneconomical. Such a firm passes what is known as the optimum point of expansion. There has been a strong tendency for American businessmen to be carried away by the idea of bigness. This was particularly true in the booming 1920's. Merger followed upon merger and expansion followed expansion to the point where many firms had passed their most economical size. In the depression which followed, huge organizations were operating at 40, 30, or 15 per cent of capacity, while some of the smaller firms continued operations as usual. All of this goes to show that mere size is no assurance of economy.

Even if economies do result from large-scale operations, it does not necessarily follow that they are passed on to consumers in the form of lower prices. The corporate form of organization is admirably suited to manipulation designed to increase profits for a few officials at the expense of stockholders as well as consumers. The preceding discussion of competition reveals that apparent competition is not always genuine. This means that large-scale economies may or may not be shared with consumers.

As a final comment on the validity of this general argument it must be observed that the contention simply does not apply to those firms engaged in industries whose costs either remain constant or actually

[1] Borsodi, Ralph, *The Distribution Age*, chap. 21, D. Appleton & Company, New York, 1929.

increase as volume of production increases. These two types of industries represent a very considerable proportion of American manufacturing enterprise, to which this argument for advertising does not apply. Moreover, it is not uncommon for firms whose costs do increase to advertise extensively. The Bell Telephone Company, for example, insists that it is a business of increasing costs, yet it advertises extensively for new business.

Indirect Benefits. Consumers are told that not only does advertising not cost them anything but on the contrary it brings them lower prices directly in the merchandise they buy and indirectly in the newspapers and magazines they read and in the radio programs to which they listen. There can be no doubt that as at present organized in the United States the advertising budgets of those who have things to sell are used to provide free radio entertainment for those who are potential buyers. Whether this situation is preferable to other possible arrangements for providing radio entertainment is a controversial point, the merits of which cannot be evaluated in this discussion. Consumer buyers are told also that their magazines and periodicals cost them much less than they would if there were no advertising carried in the periodical. It has been estimated that in 1935 one fifth of the total advertising outlay was returned to consumers in the form of lower cost for publication and radio entertainment.[1] If the same ratio was valid in 1943 that would mean that $426,000,000 worth of publications and radio was returned to consumers that year. In 1943 $890,000,000 was spent for newspaper and periodical advertising. This is the equivalent of $6.55 per capita. It means that for $6.55 more per person newspapers and magazines could have been had without advertising. There can be no doubt that the $890,000,000 paid to publishers by advertisers made it possible for publishers to charge subscribers lower prices. To the extent, however, that subscribers are also buyers of other commodities it means that they pay more for those commodities in order to get their publications at a lower price. What this means can be illustrated. The people who use headache remedy pay a price which includes enough to pay the newspaper publisher, who therefore charges them a lower price. Those who do not use headache remedy get cheaper newspapers at the expense of those who do. If the unsubsidized price of a newspaper should be five cents, users of headache remedy and all other buyers of advertised merchandise would be ahead in the long run if they paid five cents for their newspaper and proportionately less for their headache remedy. It is well to remember that one rarely gets something for nothing. If newspaper and periodical subscribers get their publications for less

[1] BORDEN, *op. cit.*, p. xxvi.

than cost it is only because they pay more for some of the other things they buy.

Another indirect benefit which might be claimed for advertising is that it helps to maintain democracy in our economic system. It is argued, by analogy, that campaigning for political office is really advertising for votes and that such advertising is essential to political democracy. Likewise it is said that advertising for buyers is like campaigning for voters and is essential to democracy in the market place. The cost of political campaigning has always been one of the most serious problems in political democracy and one which voters have attempted to control. It is known that not infrequently many times the annual salary for political office is spent to secure election to that office. This means that what might be called political advertising may very easily become a factor in destroying real democracy as a whole. Likewise with economic advertising: to the extent that individuals are persuaded by advertising and become habitual users of certain branded merchandise, they are deprived of their freedom of choice, the counterpart of their freedom to vote. There is much more that might be said and perhaps should be said on this point, but it is necessary to move on with the observation that both political and economic advertising should be tolerated just so long as the material in both cases is informative. To the extent that it departs from the informational role and depends upon emotion and persuasion it becomes an instrument of remote control.

Summary

It pays producers to spend millions of dollars annually proclaiming their wares, because consumers do not know definitely what they want, and are amenable to suggestion and persuasion. Advertising expenditures are counted as business costs by producers, but are not considered as costs by consumers who really pay the bills. If advertising does help consumers any benefit is incidental, for its main purpose is to benefit producers. A number of consumer benefits are claimed for advertising. These include the assertions (1) that information is given to consumers concerning goods available, prices, discovery of new products, and discovery of new uses for old products; (2) that by making use of this information competition may be made more effective as a defender of consumer interests; and (3) that advertising, by increasing sales, results in large-scale production with consequent economies which are passed on to consumers in the form of lower prices. The informational claims are more valid than the others, but all are subject to qualification and modification. The last two claimed benefits particularly are more apparent than real.

QUESTIONS FOR DISCUSSION

1. Is it true that "it pays to advertise"? Whom does it pay? And *who pays?*
2. Is it logical to accept the assertions of a seller that his wares are the best?
3. Why do we consider advertising by professional men unethical?
4. Why do we tolerate advertising and condemn the man who "blows his own horn"?
5. Do advertisers have a property right in your buying habits, because they have influenced them by advertising? Who paid for influencing your buying habits?
6. Do you know of any cases of advertiser control of a periodical or newspaper?
7. To what extent are newspapers and magazines subsidized by advertisers?
8. To what extent are newspapers and magazines subsidized by low postage rates? Would you favor higher postage rates for second and third class mail?
9. What are the purposes or objectives of advertising? Do you think one of them is to help consumers?
10. In what ways is it claimed that advertising is helpful to consumers? Are the claims valid?
11. How can a holding company make pseudo competition appear real?
12. Does advertising increase or reduce prices?
13. Why do telephone companies advertise?
14. Do you think advertising in your college newspaper or annual pays?
15. How does the practice of modern advertising fit into the principles of economics as expounded by your college text?

PROBLEMS AND PROJECTS

1. Write out what you consider to be a standard for good advertising from the consumer point of view and then submit six advertisements taken from current periodicals or newspapers which meet your standard and are helpful to you *as a consumer;* compare advertisers' claims with Consumers Union or Consumers' Research reports on the advertised articles.

2. Classify the articles advertised in the current issue of *Saturday Evening Post*, of *Life*, of *Good Housekeeping*, of *Woman's Home Companion*, or some similar periodical, among wealth, nealth, and illth.

3. Compare the advertisements in a popular periodical with those in a scientific or trade journal.

4. Prepare a questionnaire and submit it to 50 members of your student body to discover the influence of advertising on their choices of such articles as toothpaste, shaving cream, face powder, cigarettes.

11

Producer-Made Wants: Advertising (Continued)

Consumers' Case Against Advertising

From a consumer point of view the really significant question concerning advertising is what it actually does rather than what it might do under assumed conditions. It has been shown that advertising can perform several useful services. In an economic system organized with the primary objective of producing for welfare rather than profit, advertising would play an important part. Its informative and educational functions would be expanded, while its emotional appeals would be curtailed. This would result in a considerable reduction of the national advertising bill. This suggests the consumers' major criticism of current advertising practice. If the consumers' case against advertising can be condensed into one sentence it would be that they do not get their money's worth because so much advertising as carried on is wasteful.

Misdirected Advertising. The first consumer criticism of advertising is that so much of it is misdirected. Advertisers themselves are keenly aware of this problem. They are constantly struggling to find effective channels of contact. Since women do 80 per cent or more of the retail buying, all avenues of approach to their minds are sought by advertisers. This explains why a mazagine like *Good Housekeeping*, with a national circulation, is practically an advertisers' handbook. Yet even in such a case a large part of the audience which many advertisers hope to reach is missed.

If consumers merely read and listened to all advertisements entering their homes, their time would be quite fully occupied. In reality they read and listen to only a small part of them. This means that a large portion of advertising literature never reaches its objective. Both from producer point of view and from consumer point of view it is wasted.

All advertising media are chance channels for reaching consumers. This is of course more true for some types than for others. A vast amount of direct-by-mail advertising is doubtless thrown into wastebaskets without being opened. Much door-to-door advertising is equally futile. Billboard and highway advertising cannot possibly reach more than a

small percentage of potential consumers. The air is so filled with radio advertising that there is no way of telling whether a particular announcement reaches potential buyers. Effectiveness is dependent not only upon interest and attentiveness of listeners but also upon mechanical limitations in sending and receiving sets which are beyond the control of advertisers. Differences in time render a program less effective in one locality than in another. So also do differences in climate. Much newspaper advertising is lost on many readers. Men turn to the sports page, women to the women's page, and children to the funnies. They rarely turn deliberately to advertising columns. It is claimed that comics attract 99 per cent of juvenile readers, 72 per cent of adult female readers, and 68 per cent of adult male readers. Such advertisements as they do read are incidental. This is true also, though perhaps to a smaller degree, in the case of magazines. These are more likely to be published for a special group of readers.

While there is no way of estimating the volume of misdirected advertising, the sum total must be very large, and represents sheer waste.

Useless Advertising. Even though properly directed, much advertising is useless. Instead of supplying consumers with useful, reliable information it is obviously biased. In some cases it is downright deceptive. One of the first principles of many advertising agencies seems to be to minimize information and maximize emotional appeal. In Mr. Fairbanks' opinion advertising to intelligence is passé. "College professor logic" and 100 per cent truthful advertising do not pay. "Everybody loves and hates, and wants food and shelter and clothing and to be well thought of. . . . " If advertising copy promises satisfaction of one or more of these desires "it will tend toward ringing the bell. . . . "[1] Writing of cosmetics advertising, Mr. Roger Babson says, "She pays—under the spell of hypnotic advertising—for excessively ornate packaging, for an extortionate expense of distribution, for gyps in quantities and qualities—and for the very publicity which exploits her."[2] It is obvious that the purpose of such advertising is not to benefit consumers but to use whatever means are effective to compel them to buy. As Mr. Babson puts it, advertising has "developed a mass of false standards, spurious values, and artificial appeal." Elsewhere he says that even the advertisers admit that " . . . most of these *things* which they advertise do not make people better, healthier, or happier . . . "[3] While such advertising may benefit producers it is opposed to consumer welfare and socially wasteful.

[1] FAIRBANKS, A. H., "Reason Why Copy and the Dear Old General Public," in *Printers' Ink*, vol. 121, p. 81.

[2] BABSON, Roger, *The Folly of Instalment Buying*, p. 155, J. B. Lippincott Company, Philadelphia, 1938.

[3] *Ibid*., pp. 155, 241.

Competitive Advertising. A third indictment of advertising by intelligent consumers is that much of it is purely competitive. Its purpose is merely to switch consumers from one brand to another or from one product to another. This type of advertising is well illustrated by efforts of cigarette manufacturers to induce smokers to shift from one brand to another or to forgo candy in favor of tobacco. No one, it will be noticed, makes any effort to inform consumers that they might very well dispense with both products.

While Mr. Calkins admits that "matches already have 100 per cent distribution and 100 per cent consumption," he contends nevertheless that at present the match market is everybody's market, since there is no extensive advertising in the field. It is his suggestion and prediction that some smart manufacturer will pre-empt the match market by adopting a distinctive trade name and spending thousands or millions of dollars in a national advertising campaign designed to convert all match users to his particular product.[1] Nothing could illustrate better the individual outlook of advertisers in contrast to the social point of view. No more matches would be consumed nor would better matches be produced. There would be no increase in welfare of consumers. The net result would be a higher price to buyers for the purpose of swelling manufacturers' and advertisers' profits.

It must be admitted that there is opportunity for performing a useful service by inducing buyers to increase their utility by consuming less of some commodities and more of others. Americans are inclined to eat too much sugar and meat, while their diets are deficient in milk, fruits, and vegetables. Yet a producer of any one of these latter products stands to gain or lose according to the success of his advertising campaign. He is scarcely the one whose advice should be followed unquestioningly by consumers. Millions of people have been convinced by the advertising of certain fruit growers not only that their systems require iron but that raisins are the only reliable source of that mineral. While that is not true, many consumers have no way of knowing it. Other foods, such as prunes, spinach, and carrots, are rich in iron content. When the National Dairy Council urges consumers to drink more milk it is performing a useful service even though that is incidental to its main purpose.

Deceptive and Misleading Advertising. A fourth count against advertising is that much of it is deceptive and misleading. Until March 21, 1938, there were practically no legal restraints on advertisers; and one might have advertised that cream cheese would cure tuberculosis or that dated coffee would insure marital happiness. Until then all efforts effectively to

[1] CALKINS, E. E., in SHELDON and ARENS, *Consumer Engineering*, p. 9, Harper & Brothers, New York.

define and limit advertising claims by statute had failed. Common law theory that advertising is merely trade puffing of wares still prevailed. Such puffing is not in the nature of a warranty, so the advertiser could not be held responsible for anything he said. As the Pure Food and Drugs law was then written, the Federal government had authority to prevent or to penalize interstate shipment of foods and drugs whose labels contained false, misleading statements. Producers of inferior food products or quack medical preparations therefore had to be careful in writing the label, but were not held responsible for misstatements made in supplementary advertising. Since most consumers are influenced much more by advertising than by mere statements on labels, the net result was little or no protection for unwary buyers.

Since there was no legal regulation of advertising it was—and still is—difficult to convince consumers that some advertising is false and deceptive. This is because there is usually no standard by which to judge it. Whatever the producer says about his product is difficult to challenge authoritatively. Gullible consumers are easily convinced that whatever an advertiser says must be true or else he would not say it. Although the schools have taught the technique of advertising "they have not taught adequately how to *read* advertising—how to read it with liberal discounting of claims and healthy skepticism of promises."[1] Yet consumers are not wholly without protective guides. One of these is *Notices of Judgment*, issued by the Food and Drug Administration and a useful guide in addition to the new law.

One of the "greatest discoveries" issuing from the first World War was introduced to American sufferers from common colds by a national advertising campaign describing the remarkable curative properties of Vapex. Readers may recall the full-page advertisements announcing this new boon to suffering mankind. So enthusiastic were the producers that they overstepped legal limits at least three times within five years. In half a dozen states shipments of Vapex were seized by government officials who alleged that the product was misbranded and that statements on the labels were false and misleading. Analysis revealed that the product was an alcoholic solution of oil of lavender, oil of eucalyptus, and menthol, containing approximately 66 per cent alcohol and water. A statement that it was produced in England was false since a part of the manufacturing process was carried on in this country. In defending the case the American agents presented the naïve argument that Vapex is not a drug within the meaning of the law and that "it is a harmless substance in no way detrimental to the public health." While the producers made bold claims in their advertising, the most they would

[1] BABSON, *op. cit.*, p. 113.

claim in court was that Vapex is innocuous. No attempt was made to demonstrate its positively beneficial properties.[1]

Within recent years the manufacture and sale of vitamin preparations have become a big business. In 1925, the first year for which figures are available, retail sales amounted to $685,108. The estimated volume of retail sales for 1942 was $130,896,000.[2] Advertising has been used extensively but not always accurately. *Notices of Judgment* for March, 1943, contains several cases dealing with adulteration and misbranding of vitamin preparations. A shipment from New York to Baltimore was subjected to libel on the charge that the labeling "bore false and misleading claims regarding its efficacy to restore and maintain health and prevent or correct diseased conditions." Statements in an accompanying circular entitled "What You Should Know About Vitamins" represented, suggested, and created in the mind of the reader the impression that health could be assured by consuming the advertised pills; that the average individual requires supplemental vitamins to maintain maximum health; that he is likely to be suffering from lack of vitality, lack of energy, poor appetite, and impaired digestion because of inadequate vitamin intake; that if the pills were consumed as directed they would prevent or correct diseased conditions resulting from vitamin deficiency. As a matter of fact, the product could not have fulfilled all of these claims even if it had been all that it purported to be. Actually, it did not contain riboflavin or nicotinic acid, both of which are essential in normal nutrition. The shipper admitted all the charges in the libel, whereupon a judgment of condemnation was entered and the product was ordered released under bond to be relabeled. It was required further that the circular entitled "What You Should Know About Vitamins" be removed from the carton.[3]

Another helpful guide in checking advertising claims is the *Monthly Summary of Work* of the Federal Trade Commission, available upon request. It lists the names of firms which have been ordered to cease and desist from misrepresenting their products. It also lists the names of firms which have agreed in stipulations to cease representing certain claims to which the Commission has taken exception. More complete accounts are to be found in Federal Trade Commission *Decisions*. Since 1938 many well-known firms who use advertising extensively have either agreed to stop certain advertising misrepresentations or have been ordered to do so. The selling corporation for a cosmetic firm agreed to

[1] Department of Agriculture, Food and Drug Administration, *Notices of Judgment*, Cases 20371, 21230, 22576.

[2] "Vitamins Go To War," in *Business Week*, July 10, 1943, p. 59.

[3] Federal Security Agency, Food and Drug Administration, *Notices of Judgment Under the Federal Food, Drug, and Cosmetic Act*, March, 1943, Case 3644.

stop advertising that certain of its products would remove brown spots, freckles, or other discolorations; a national advertiser agreed to stop representing that its facial cream would restore oil to the skin, and so on through thirty stipulations; another firm, together with a long list of holding company subsidiaries in Maryland, New Jersey, California, Tennessee, and so on, was ordered to stop representing that any of its products originated abroad unless they actually did so; another agreed to stop advertising that its various cosmetic products would affect the contour of the face, and so on through twelve stipulations; the sales corporation for another firm was ordered to stop advertising that its facial powder would do any one of four things claimed for it; and a final example is that of a firm ordered to stop advertising that any of its preparations would nourish the skin muscles or tissues, and so on for a number of additional stipulations.[1] Similar records are to be found in Federal Trade Commission *Decisions* for national advertisers of dentifrices, gelatin, food products such as flour and cereals, soap and soap products, medicinal preparations, and so on through a long list of nationally advertised articles.

Although the Federal Trade Commission *Monthly Summary of Work* is released to the press very few newspapers or periodicals publish the contents of the *Summary*. In the summer of 1943 *Reader's Digest* started publishing each month a summary of Federal Trade Commission actions against the manufacturers and advertisers of such products as cigarettes and dentifrices. If this is continued consumers may use *Reader's Digest* as a source of information concerning the work of the Federal Trade Commission and the validity of the advertising claims carried in the press and over the radio. The advertising trade papers expressed great indignation that *Reader's Digest* should print such information for its readers, to which the editor replied that in his judgment exposure of the abuses of those who misuse advertising will have a salutary effect. Moreover, he added, advertising copy of the type proceeded against by the Commission is detrimental to all advertising.[2]

As a third useful guide for checking advertising claims, increasing numbers of consumers are using the annual *Buying Guide* of Consumers Union and the *Handbook of Buying* issued by Consumers' Research, Inc., together with each organization's regular *Reports*. The work of these organizations will be described more fully in Chapter 17.

[1] Federal Trade Commission, *Decisions*, vol. 33, Case 02873; vol. 27, Case 02191; vol. 29, Docket 3325; vol. 28, Case 02357; vol. 33, Docket 3438; vol. 33, Docket 4244; and vol. 27, Docket 2939.

[2] Clark, Blake, "Lifting the Cigarette Ad Smoke Screen," in *Reader's Digest*, July, 1943, pp. 17–21; and "Taking Dentrifice Ads to the Cleaners," August, 1943, pp. 19–23; also *Advertising Age*, August 2, 1943.

A fourth guide which consumers may use is their own well-developed common sense. Merely to read or to hear the absurd and silly claims made by many advertisers should be enough to render them suspect. Yet "there is one kind of advertising which never fails, and that is the relief of sickness and suffering before one's very eyes. Upon that kind of advertising, B & M depends more than upon anything else." B & M is a product consisting of "approximately 42 per cent turpentine oil, approximately 5 per cent ammonia, small proportions of ammonium salicylate, hexamethylenamine, thiosinamine, and a phenolic substance such as cresol, albuminous and phosphorus-containing material such as egg, and water."[1] Producers of preparations like this may claim for them power to cure all human afflictions even though reputable medical practitioners admit that for some ailments such as cancer they know of no sure cure.

Advertising Nealth and Illth. Fifth among consumers' complaints against advertising is that such a large proportion of it seeks to sell products whose ability to contribute to the welfare of consumers is at best questionable. In the words of one businessman critic, "one of the severest indictments of advertising is based on its tendency to corrupt the public's desires."[2] Depending upon one's standards, some advertised products are positively harmful, and some are potentially harmful, while others are innocuous. The innocuous products would be nealth, as they neither benefit nor harm the consumer. The net result of their advertising is to transfer purchasing power from those deceived to the deceiver. *Notices of Judgment* are filled with thousands of cases of quack and adulterated products all of which are advertised, some on a national scale. Warm Springs Crystal Compound was labeled to convey the impression that it consisted of minerals obtained by the evaporation of water from Warm Springs, Georgia, made famous as a health resort by President F. D. Roosevelt. Analysis showed that the article had not been produced from Warm Springs water but was merely ordinary Glauber's salt, which is sodium sulphate decahydrate. The labeling of the product also contained unwarranted curative and therapeutic claims.[3]

Thumbing through familiar advertisements which appear regularly in magazines, one may find additional illustrations of advertised illth or nealth. There is, for instance, much advertising of dentifrices, each designed to convince consumers that it is absolutely essential to oral hygiene. The fact seems well established that none of these highly advertised preparations can do more in the care of teeth than a simple solution

[1] Department of Agriculture, Food and Drug Administration, *Notices of Judgment*, Case 19651. [2] BABSON, *op. cit.*, p. 154.

[3] *Notices of Judgment*, Case 22613.

of salt and water. Return of legal liquor has resulted in an avalanche of advertising which may be beneficial to distillers and publishers but scarcely to consumers.

Advertising the Merits of Competitive Consumption. A sixth criticism of advertising, from a consumer point of view, is its increasing tendency to stimulate and encourage artificial and competitive consuming habits. The new doctrine of obsoletism is fostered by self-styled consumer engineers. It is a high-sounding title for advertising designed to make people so dissatisfied with what they have that they will proceed to junk it and purchase the latest model or style. "We must no longer buy a house to live in until we die; a refrigerator to last until it falls apart, an automobile until it refuses to go, a radio that simply brings in one or two stations." What would happen if women wore their clothes until they were frayed? Advertisers ask and answer this question. In their judgment "it would well-nigh ruin business." The good old days when boys wore father's cut-down pants are over. The making of boys' clothing has become an industry. So argues the consumer engineer.[1] By implication it is not the function of the industry to make clothing which will satisfy consumers' wants, but it is rather the function of consumers to buy and discard at such a rapid rate as to assure profits to clothing manufacturers. The whole philosophy of consumer engineering reverses the traditional consumer-producer relation. In attempts through advertising to foist on consumers businessmen's philosophy of profit, consumers become no more than a tool whose function is to increase producers' incomes. The test of utility to consumers gives way to the test of profit for producers. "Goods fall into two classes, those we use, such as motor cars or safety razors, and those we use up, such as tooth paste or soda biscuit. Consumer engineering must see to it that we use up the kind of goods we now merely use."[2]

Fashion, custom, conspicuous consumption, and emulation have been capitalized by advertisers seeking to compel consumers to conform to false standards. Advertising has become a means of keying consumption to the modern tempo of living. Its purpose is to create dissatisfaction rather than satisfaction. So operating it becomes an effective means of encouraging consumers to live beyond their incomes by resorting to installment buying.

Advertising Decreases Production. Critical consumers' seventh objection to much current advertising is that it results in an actual decrease of wealth produced. Stuart Chase once estimated 600,000 persons were

[1] Frederick, J. George, *A Philosophy of Production*, p. 168, The Business Bourse, New York, 1930.

[2] Sheldon and Arens, *Consumer Engineering*, p. 13, Harper & Brothers, New York.

engaged directly or indirectly in advertising. He estimated further that the efforts of perhaps 10 per cent of that number resulted in genuinely useful services to consumers. That meant that 540,000 workers could have been dropped from industrial payrolls without in any way diminishing the amount of actual wealth produced. Still more significant is the possibility of redirecting the efforts of these half million workers into channels which would result in real wealth. Thus viewed, advertising actually decreases wealth production.

Immediate objection would be raised to this contention on the basis that we normally have so many unemployed that it would be impossible for another half million to find opportunity for useful as well as gainful occupation. This is perhaps true under a profit economy. This is not to contend, however, that it would necessarily be true in an economic system organized on the assumption that the main purpose of production is to satisfy human wants. If production for use were to displace production for profit, unlimited human wants would afford ample outlet for man's ingenuity and creativeness.

Professor Borden would doubtless say that the foregoing statements are based upon theoretical analysis which assumes full employment of all resources. He suggests that if we accept the doctrine of Lord Keynes that equilibrium may be attained below full employment it then follows that advertising is a means of helping to reduce chronic unemployment. This would be accomplished *if* advertising would lead to a demand for new products which in turn would call forth new investment.[1]

Recent developments in economic thought have stressed the decline of price competition in the 1920's and 1930's and the rise of non-price competition. Concomitant with that development was the growth of dominance of a small number of firms in various industries, technically called oligopoly, and the development of differentiated products, technically described as monopolistic competition. One of the most significant forms of non-price competition has been that of advertising. With its help producers have been able to gain maximum profit at a production point somewhat below that which would be achieved in a freely competitive economy. To the extent that advertising is essential to various stages of monopolistic production, it must be held responsible for the smaller output characteristic of monopolistic enterprise.[2]

Some Advertising Misuses Art and Science. Still another objection to much modern advertising is its base and unworthy use of art and science.

[1] BORDEN, *op. cit.*, pp. 185–189; pp. 868–871.

[2] For an analytical statement of this aspect of advertising see BOWMAN, Mary Jean, and BACH, George Leland, *Economic Analysis and Public Policy*, Part IV, especially chap. 24, Prentice-Hall, New York, 1943.

Although this may not be considered strictly an economic objection it is nevertheless important in the judgment of critical consumers. Advertising has gone far in placing the dollar sign on art. Much of it succeeds in twisting art for art's sake into art for the sake of profit. Promising artists for whom the capitalist system makes no provision are lured into commercial art by prospects of rich returns. Something might be said for advertising if it operated to subsidize real art, but wide appeal is made more effectively in the judgment of advertisers by perverting recognized art to ulterior purposes. Sex appeal is perhaps the most common characteristic in commercial advertising art. In the absence of deliberate debasement, much that passes for art in advertising is downright ugly. Touched-up photographs of pimply faces, reproductions of fear-ridden faces of halitosis sufferers, or paintings of sour-faced sufferers from jangled nerves caused by consuming unadvertised coffee or cigarettes are scarcely worth the efforts of potential artists. Probably typical girls' heads on magazine covers are considered the height of achievement of pecuniary art. Billboard advertising destroys natural beauty to replace it with man-made ugliness.

Pseudo science is used in much the same manner for the sake of profit Two words which mightily impress American consumers are "efficiency" and "scientific." If advertisers merely assert that scientists affirm the efficiency of their product, bells of cash registers will ring. Popular conception of a scientist dresses him in a freshly laundered white coat and places a test tube in his hand. Refusal of the American Medical Association to allow its members to sell their opinions to advertisers does not daunt the advertising profession. It merely reserves the American market for unknown self-styled European medical specialists. Chemists and physicists are paid to make elaborate tests, but producers reserve the right to publicize only those portions favorable to their product. In a national campaign an advertiser informed consumers that "science finds harmful acids . . . *mercury* . . . *arsenic* . . . in many brands of toilet tissue." It was stated that 660 brands had been tested by a "nationally known laboratory." Investigation by the American Medical Association revealed many points not mentioned in the advertising. No allowance was made for differences in price nor was the public informed that in some respects other papers were superior to that of the advertiser. For example, no more wood fiber was found in 55 per cent of the 660 brands than in the advertised brand, while three of the brands had fewer splinters and six of them contained no splinters at all. Less than twelve of the 660 brands had any arsenic, and those in such infinitesimal quantities as to be insignificant.[1]

[1] *Journal of the American Medical Association*, July 16, 1932.

In the judgment of one scientist, cigarette advertisements "broadly and generally speaking . . . are . . . ridiculous and shameful distortions and prostitutions of scientific thought and method."[1]

The imitative instinct is capitalized and commercialized by advertisers. Common consumers are impressed by what social leaders may use. If they say it is "X Cream" which preserves their complexions, presumably millions of women will use the same product even though X Cream has to pay $1,000 to one social leader, and $3,000 to another, for their endorsement.

Copy writers are advised not to know too much about the product for which they are writing. Mrs. Woodward said to her copy writers, "Never see the factory in which it is made, don't know too much about it . . . because . . . when you know the truth about anything, the real, inner truth—it is very hard to write the surface fluff which sells it."[2] As a result engineers who have created certain products would hardly recognize some of them from what the copy writers say.

Psychology has become a pillar in the advertising temple. Advertisers have not hesitated to turn this science to commercial purposes. They have searched the field so thoroughly and extensively that they have developed a special psychology of advertising. This is sufficiently important to justify special attention in the following section.

Dissecting the Mind of the Buyer

Advertising Psychology. Comparison of early advertising with that of today reveals its former crudeness and ineffectiveness. Much of it was simply naïve. Modern advertising began when advertising agencies dropped their rule-of-thumb methods and spontaneous hunches for the established principles of psychology. They combined the determination of businessmen with the precision and the skill of psychologists to dissect the mind of the buyer. Their purpose was to discover consumer weaknesses that might be capitalized. They operated under no illusions or restrictions concerning a higher purpose for psychology. Since then the literature of advertising and selling psychology has grown apace. With new tomes annually revealing new lines of attack, the scalpel of psychology has laid bare to all advertisers the innermost secrets of the buyer's mind. As new points of vulnerability are discovered still others are eagerly sought.

One of the first psychologists to recognize the trend was Professor Kitson, who wrote the following significant sentence in 1920: "They

[1] Solomon, Charles, *The Traffic in Health*, p. 284, described as a physician's personal account of the existing fraud in patent medicine and cosmetics, Navarre Publishing Company, New York, 1937.

[2] Woodward, Helen, *Through Many Windows*, p. 298, Harper & Brothers, New York.

[businessmen and teachers of future businessmen] are determined to wrest from the science [of psychology] every item that will serve them in the manipulation of human conduct." He hoped for that reason "to keep psychological principles and methods from being garbled and distorted by well-meaning but blundering laymen," and assumed "that no reader will undertake any practice which is not ethically justified."[1]

The verdict of a generation of advertising growth is that neither of these assumptions was justified. Blundering laymen were not even well-meaning; they garbled and distorted principles of psychology for their own selfish interest. Advertising copy and selling methods have been used which cannot be justified ethically.

The psychology of selling recognizes the following stream of thought leading up to a sale: Attention, Interest, Desire, Confidence, Decision, Action, and Satisfaction. The first task of selling is to attract attention. This may be accomplished in a number of ways. It may be done by thrusting something into the thought stream of consumers which is sufficiently intense to drive out every other thought. Big billboards, blustering radios, and brilliancy in color are suggested by psychologists as effective means of attracting attention. An advertiser may appeal also to American proclivity for bigness. This is particularly effective on American buyers who associate bigness and quality. The alliterative phrase "bigger and better" is characteristically American. Psychology has discovered that the human mind is powerfully affected by movement and therefore suggests increased use of moving signs. This also suggests Kitson's conclusion that "the cinema as a selling medium has not yet come into its own."

Parenthetically, it may be observed that during the many years since Kitson wrote there has been remarkably little development in the use of moving pictures as an advertising medium. Perhaps this is to be explained by the fact that the audience, having paid for admission, will not tolerate dull advertising notices. There is of course a great deal of indirect advertising in regular pictures, yet it is surprising that more purely propaganda films have not appeared. If the advertising fraternity once makes up its mind to invade this field, moving pictures may go the way of radio. Then consumers would no longer buy tickets of admission to moving picture theaters but would get their movies "free" by purchasing advertised merchandise.

An interesting experiment in the use of films as advertising media was made in New York. Under direction of the Yale Child Clinic, Arnold Gesell, professor of psychology, prepared a series of films showing

[1] Kitson, Harry D., *Manual for the Study of Psychology in Advertising and Selling*, pp. 5, 8, J. B. Lippincott Company, Philadelphia, 1920.

child development from one week up to sixteen years. These films were shown by retail merchants, usually in their own buildings. There was no direct selling effort, but the film did suggest to mothers types of clothing, playthings, and accessories which they should purchase for their children. Those in charge of the experiment emphasized, as did Professor Kitson years ago, the importance of maintaining education as the dominant theme and of excluding all selfish sales appeal. Whether or not this advice will be heeded and whether such films will become important advertising and selling media remain to be seen.[1]

Returning to the psychologist's suggestions for attracting consumer attention, another suggested means is change, and still another is use of color, of which there are 30,000 varieties, with red, green, blue, and yellow most preferred. The final suggestion is that in case all these other means fail then "mere bald, brutal repetition goes far in attracting attention," because "man is innately credulous" yet as he grows old he develops inhibitions which make him resist. Consequently repeated statement is necessary to overcome this acquired resistance. This psychological characteristic is the basis for and justification of display advertising.[2]

Psychologists emphasize the importance of choosing proper media for attracting attention. It seems quite obvious that if advertising copy appears in *The Christian Century* it will reach a totally different class of readers than if it appears in *The New Yorker* or *Esquire*. One of the first principles of psychology in advertising was that attention once attracted could be held best by developing a feeling of good will between prospective seller and buyer. In developing this feeling humor has proved strikingly ineffective. Yet there has been a noticeable revival of the use of cartoons in magazine and newspaper advertising. The *Comic Weekly*, distributed through seventeen Hearst Sunday papers, advertised for advertisers by claiming a reader list of 20,000,000. It exhorted advertisers to "make them laugh; make them cry; thrill them; talk to them of love . . . the way to the family pocketbook is straight through the heart."[3]

Starting in New York, women in 39 states organized themselves into groups to boycott objectionable radio programs. Their slogan was "I'm not listening." Appearing before one of these groups a radio official is quoted as having said, "We are in the broadcasting business to make money and gripping dramas pay for the worthwhile programs that don't pay their way." He admitted that it might be a "sad commentary but it was a fact that a leading soap company had found through surveys

[1] The films are released through Encyclopaedia Britannica Films, Inc., New York.
[2] KITSON, *op. cit.*, pp. 44, 45.
[3] *New York Times*, p. 19, October 1, 1935.

that the radio program public listens to serial stories and that they sell soap."[1]

Advertising copy having attracted attention must proceed to maintain consumer interest, to develop desire, to instill a feeling of confidence leading to decision, culminating in the act of purchase.

High-Pressure Selling. High-pressure salesmanship goes hand in hand with advertising. In fact advertising is merely a special form of high-pressure selling. Mrs. Woodward presents a striking picture of the high-pressure methods used in selling a world history. In order to make a profit on some kinds of books a publisher must sell hundreds of thousands. To do that "it is necessary to force the sale; to be so persuasive in advertising that you will induce people to buy your books who had no interest in them before." In her judgment "the average successful salesman is gregarious, talkative, cordial. A spectacular appearance is a help." Still another important characteristic is necessary. "The best salesmen," writes Mrs. Woodward, "are impervious to insult, utterly indifferent to the desires of others. It is a nuisance when you are trying to sell a man a large bill of goods to have the thought come into your mind that it is an unkind thing to force the goods on him. If that thought comes too persistently you don't sell."

Mrs. Woodward reports that one of the publishers' super-salesmen earned $35,000 a year by selling books that were overpriced to people who did not want them, by a method thus vividly described: "Do you see how I am looking at you? If I kept it up I could make you do anything I wanted. That is the way I look at them. . . . I hypnotize them. I hypnotize them. Until they sign on the dotted line they're my slaves and my servants."[2] Such is the use to which the science of psychology is put.

The Advertising Agency

How It Works. One of the peculiar features of advertising is the advertising agency. Those untutored in advertising procedure might naturally think that when a producer reaches a decision to advertise, some member of his own staff familiar with the product prepares the copy and arranges for its publication or broadcast. Except in rare instances nothing could be further from the truth. In the 1860's an advertising agent was primarily a jobber of newspaper space. Oftentimes he purchased space in bulk quantities and then sold it to advertisers. Beginning in the 1890's the advertising agent began to write the advertiser's copy as well as to place it for him. Most advertising agencies have

[1] *New York Times*, March 16, 1940.

[2] Woodward, *Through Many Windows*, pp. 74, 94, 227, 274, Harper & Brothers, New York.

continued as space-jobbers. Instead of being paid by the firm whose product is advertised, they receive a commission from the publishers on all advertising space which they sell. The customary commission is fifteen per cent. The effect of this arrangement is a consequent urge by agencies to influence producers to increase their advertising appropriations. In the words of one of the many critics of this system it "makes for waste, private rebate, and special arrangements between one group and another." Manufacturers are increasingly resentful of it.[1]

Perhaps the first firm to break away from the usual commission basis was N. W. Ayer & Sons of Philadelphia, who inaugurated the open contract with the advertiser in 1870. Under that plan the advertising agency receives from the advertiser as a commission or fee 15 per cent of the gross advertising appropriation. While this is an improvement it still retains the feature of basing the charge for services on the cost of space used and creates the temptation on the part of the agency to urge the customer to spend more money on space than might be wise or necessary.[2]

The more accounts an agency secures the more space it purchases from publishers and the larger are its commissions. This leads to wasteful competition among agencies for new accounts like the two following cases described by Mrs. Woodward. In 1923 the Frank Presbrey Agency was one of nineteen competing for the Buster Brown Stocking account. Only five concerns were asked to submit plans and bids, but the other fourteen were so eager to secure the business that they submitted unrequested plans. Expenditures in drawing up proposed advertisements ranged from a minimum of $500 to several thousands of dollars.

In 1912 the Presbrey Agency entered competition for the H. J. Heinz Company account. Mrs. Woodward describes in detail her weeks of planning a campaign, which cost her agency $1,000. The net result was purely negative. When the carefully prepared, attractively bound prospectus was submitted, eccentric Mr. Heinz refused even to look at it, because he did not like Frank Presbrey.[3] This is an excellent illustration of competitive advertising waste. Considerable waste is involved in unnecessarily advertising food; more waste is incurred by the competition of advertising agencies to secure the account; the final waste is failure of the manufacturer even to consider the plan. That this practice is not uncommon is attested by evidence of other former copy writers.[4]

[1] *New York Times*, February 1, 1939.

[2] HOWER, Ralph M., *The History of an Advertising Agency, N. W. Ayer & Sons At Work, 1869–1939*, chap. 3, pp. 83, 85, Harvard University Press, Cambridge, Massachusetts, 1939.

[3] WOODWARD, *op. cit.*, pp. 213, 214.

[4] RORTY, James, *Advertising: Our Master's Voice*, chap. 4, John Day, New York, 1934.

Advertising Appeals. Whether the approach to consumers is made directly by salesmen or indirectly by advertising, psychology reveals the most impressionable appeals. Lucas and Benson have classified advertising appeals as follows:[1]

- I. Personal
  - A. Individual
    - Appetite—taste
    - Success—power
    - Possession
    - Wealth—independence
    - Beauty
    - Cleanliness
    - Health
    - Comfort
    - Play
    - Fear—avoidance
  - B. Social
    - Popularity
    - Sex—mating—parental
    - Rivalry
    - Domination—submission
    - Conformity and distinction
    - Sociability—hospitality
    - Co-operative or altruistic
- II. Objective
  - Quality—size
  - Beauty—appearance
  - Price
  - Prestige—age of business
  - Recommendations and testimonials

Producers of food generally appeal to appetite, taste, and health; correspondence and business schools and colleges appeal to human desire for success and power; banks and investment companies appeal to the longing for wealth and independence; soap and cosmetic manufacturers appeal to desire for beauty, cleanliness, health, and comfort; manufacturers of sporting goods appeal to the play instinct; producers of firearms, tires, flashlights, and insurance salesmen appeal to the fear instinct. So on throughout the list, advertisers select particular appeals which are likely to break down resistance to sales efforts. In the absence of social control advertisers grow bolder in their appeals. No human emotion is too delicate or personal for commercialization. Supposedly family magazines carry advertisements which appeal so obviously to sex instincts that thoughtful parents must feel concern over the effect on adolescent members of the family. Advertising of toilet tissue, women's

[1] LUCAS, D. B., and BENSON, C. E., *Psychology for Advertisers*, chap. 5, Harper & Brothers, New York, 1930.

accessories, and other personal requirements has become so suggestive as to cause embarrassment in calling them to the attention of members of mixed groups. Federal laws prohibit dissemination of information concerning contraception, yet pages of "respectable" magazines carry advertisements which by implication and suggestion urge the use of certain proprietary products for contraceptive purposes.

Fear advertising has been one of the main supports of quack practitioners and producers of patent medicines. To some advertisers mother love is a convenient means of compelling women to buy their products. Mrs. Woodward received the following instructions from the manager of the advertising agency for which she worked. "As for this baby food stuff, for God's sake put some sob stuff in it. You know. And make it beautiful too. Make it beautiful, make the words sing. Heavens! There isn't a woman in the world that cares about facts. That kind of stuff you write for the *Woman's Home Companion*, that's what gets 'em. Tears! Make 'em weep. . . . If we only had the nerve to put a hearse in the ad, you couldn't keep the women away from the food."[1] Not knowing a thing about the baby food, Mrs. Woodward proceeded to write glowing copy conveniently unrelated to the facts and unhampered by truth. In later years she acknowledged publicly that she was not proud of her part in that campaign, particularly after discovering that the baby food was not nearly as good as the producer and manager of the advertising agency had led her to believe.

Earlier in this chapter it was reported that *Reader's Digest* in 1943 undertook to publicize some of the findings of the Federal Trade Commission. It is reported also that there was considerable objection among the advertisers, as revealed in the advertising trade journals. The advertising manager of a New York furniture company wrote a lengthy letter to the editor of *Advertising Age*, disagreeing with an editorial concerning the practice of *Reader's Digest*. But at one point in that letter the writer said, "Do not misconstrue these remarks as a sales talk for ethics in advertising. On the contrary, the only purpose of advertising is to improve the business of the advertiser—directly or indirectly, present or future. If this objective can be obtained only by disregard of ethics, and if it is certain that such disregard will achieve the results, then to hell with ethics. The point being made is that advertising should be divorced of exaggeration and misleading innuendos not for the sake of ethics, but for the fact of profits. Advertising to be effective, must be believed. To be believed it must be above suspicion. To be above suspicion it must be considered sincere and honest."[2]

[1] WOODWARD, *Through Many Windows*, pp. 203, 204, Harper & Brothers, New York.

[2] *Advertising Age*, July 19, 1943.

Control of Advertising

Need for Control. In a free competitive system lacking conscious control the art of advertising degenerated into competition among advertisers in promising the world and all there was in it. Untruthful and misleading advertising probably reached its height in the early part of this century. In 1906 it was estimated that 72 per cent of newspaper advertising was doubtful and that 32 per cent was definitely objectionable. Of such types of advertising exaggeration is one of the most common. An effective copy writer must possess a full vocabulary of superlatives. Regardless of the product being advertised it is described in general terms as superior in every respect. Casual comparison of advertisements in current magazines will reveal many illustrations of this type of advertising.

Another type of false and misleading advertising is commonly found in newspaper announcements of fictitious sales. Merchandise is offered for sale at prices as high as or higher than regular prices. Closely akin to this practice is that of offering merchandise of inferior quality for sale at apparent bargain prices. Consumers are peculiarly unable to detect this type of falsity, but businessmen themselves, through such organizations as Better Business Commissions, provide numerous illustrations of these practices.[1] For example, a Columbus store advertised fur coats at a price of $39.90 which were allegedly valued at $59.50, $69.50, $79.50, and on up to $179.00. The Columbus Better Business Bureau bought one of the coats, removed all identification marks, and had it priced by ten local furriers and fur merchandisers. All of them agreed that the coat was worth about $43.00. The sales clerk had said that it was a $79.50 coat and the price tag showed that figure.[2]

The use of names designed to deceive consumers into believing that products advertised are made of genuine materials is a common practice among some advertisers. The average consumer knows so little about furs, silks, or wools that he is unable to distinguish between genuine and imitation products. This is accentuated by the use of misleading trade names such as Iceland fox for lamb, fiber silk for silk, and cashmere for cotton.

Determination of some consumers to display their superiority by using imported merchandise is commonly capitalized by unscrupulous merchants. This is accomplished by the simple procedure of attaching labels indicating that domestic merchandise has been manufactured by foreign firms. Reference has been made to the use of testimonials in

[1] Starch, Daniel, *Principles of Advertising*, chap. 20, McGraw-Hill Book Company, New York, 1923.

[2] Columbus Better Business Bureau, Inc., *Bulletin*, March 5, 1941.

advertising. Experience has shown that advertisers may secure endorsements from prominent people for a sufficiently attractive price. In many cases these endorsements are used without restriction while in some they may represent the genuine statement of the endorser. So far as consumers are concerned there is no important difference. The mere fact that the endorser is the wife of a wealthy man or an expert tennis player does not render her judgment of cold creams or cigarettes particularly helpful.

Page after page of evidence might be presented further to demonstrate the prevalence of falsity and deception in past and present advertising. The reader who desires additional information may secure it from sources suggested in the footnotes of this chapter. In the end it is practically certain that all will agree with Handler's conclusion that "The seriousness of the problem of false advertising, both sociologically and financially, requires no demonstration. The toll which is assessed upon the consumer runs into the millions; the effects upon the health and well-being of the community are incapable of estimation."[1]

Attempts at Self-control. Perversion of advertising had reached such an extent by 1911 that all members of the advertising fraternity were suffering. With three fourths of newspaper advertising being classed as of doubtful veracity, consumers were rapidly developing a defense complex which led them unconsciously to discount all paid claims made by producers. As a result those who were truthful and honest in their advertising were penalized along with the unscrupulous.

It may be mentioned parenthetically that this is the logical outcome of the uncontrolled operation of competition and self-interest. As long as men can make money by such means they are promoting their own self-interest although they may be retarding human welfare. To one whose whole concern is advancement of his own economic welfare the fact that others may suffer by his acts has no deterring influence. If he is smart enough to get away with it he is the gainer and consumers are the losers.

Alarmed by the trend of events, *Printers' Ink* and the Associated Advertising Clubs of the World decided upon remedial action in 1911. "Truth in advertising" was adopted as a slogan and urged upon all advertisers. Recognizing that that alone would be insufficient, a National Vigilance Committee was organized "whose function it was to take active measures toward eliminating objectionable and dishonest advertising and to promote the establishment of a higher ethical standard." Co-operating with other agencies, this Committee has been influential not only in raising advertising standards but in securing conviction of flagrant violators of

[1] Handler, Milton, "Jurisdiction of Federal Trade Commission over False Advertising," in *Columbia Law Review*, vol. 31, p. 550.

the law. Its annual reports are a rich source of material illustrating not only accomplishments of the Committee but also the persistent prevalence of objectionable advertising.

The National Vigilance Committee was instrumental in organizing local Better Business Commissions whose main function is to be on the alert to detect and stop undesirable advertising and merchandising methods. Investigators are employed to read advertisements in local papers. Their duty then is to investigate any doubtful claims. These Commissions have been successful in ferreting out perpetrators of false advertising and initiators of objectionable merchandising methods. In some cases desired results were secured merely by investigation. In other cases established facts have been publicized to warn consumers, while in a few instances it has been necessary to resort to courts for authority to end continuance of unethical selling practices. Consumers are warned through bulletins, leaflets, radio talks, and speeches to avoid unsound and fraudulent schemes which have been discovered by the Bureau. For example, Philadelphia consumers were warned against the "Weeping Widow" racket. That is described as a selling device in which women are used to sell furniture on the pretext that they must break up their home. As quickly as one set of furniture is sold it is replaced with another and the prices are not bargains.[1]

The Better Business Bureau of St. Louis performs similar services. For example, in a special bulletin St. Louis consumers were informed that the so-called wholesale prices of a furniture show room were actually higher in some cases than the prices for comparable merchandise in established stores. The smoke problem has long been acute in St. Louis, as a result of which an anti-smoke ordinance was passed. This gave rise to many opportunities for untruthful advertising. The Bureau set up a special fuel division which handled 731 cases in 1941 and inspected 4,352 advertisements. A special bulletin was issued warning consumers against wartime gyps. Twenty-two gyps which the Bureau had discovered were listed and described.[2]

In some cases the various Better Business Bureaus are able to secure the co-operation of firms guilty of unethical advertising and merchandising practices. But in many instances all that the Bureaus can do is to warn prospective buyers and then help the victims in court. The Columbus store which advertised fur coats at $39.90 is, according to the Columbus Better Business Bureau, a chronic offender. In St. Louis, in spite of all that the Better Business Bureau could do, the complaints of

[1] Better Business Bureau of Philadelphia, Inc., *Bulletin* No. 17.

[2] Better Business Bureau of St. Louis, Inc., *Bulletin*, September 28, 1942; February 5, 1942; March 22, 1943.

laundry customers were handled so unsatisfactorily that a special bulletin was finally issued to the effect that the Bureau was powerless to do anything to remedy the situation.

Some newspapers and magazines have helped to raise standards by restricting their pages to approved advertising. This of course invests some member of the publishing firm with authority to determine what is and what is not desirable in proffered advertisements. Sometimes the most undesirable advertising can afford to pay the highest rates. Since newspapers and magazines are published for profit, their advertising managers cannot ignore monetary return. Nevertheless there has been a distinct trend toward refusal to publish extremely undesirable advertising. This does not mean that a critical observer can share the enthusiasm of advertising proponents. There is still much objectionable advertising in newspapers and magazines and over the air. Merely because a newspaper refuses to publish patent-medicine advertisements or because *Good Housekeeping* magazine assumes responsibility for all advertising in its columns, consumers have no guarantee that such advertising as is accepted is useful. While it may not be objectionable it still may not be beneficial.

The Columbia Broadcasting System has announced restrictions on advertisers using its facilities. Among the basic advertising policies thus announced are the following restrictions: Advertisers may not broadcast any false or unwarranted claims for any product or service; there shall be no programs or announcements that are slanderous, obscene, or profane; ambiguous statements which may be misleading are banned; price may not be mentioned more than twice on a fifteen-minute program, three times on a half-hour program, or five times on a full-hour program; there shall be no appeal for funds, no lottery or drawing contests, and no testimonials which cannot be authenticated; no advertiser is permitted to infringe on the rights of other advertisers through plagiarism or unfair imitation, nor may any advertiser disparage his competitors or their products; finally, no advertising matter is permitted which in the opinion of CBS may be injurious or prejudicial to its own interests, to reputable business, or to the interests of the public.

Government Control—State and Local Laws. Recognizing the ineffectiveness of purely voluntary controls, attempts have been made to compel acceptance of minimum standards by legal compulsion. Supplementing efforts of the Associated Advertising Clubs for better advertising, *Printers' Ink*, an advertising magazine, prepared the following model statute in 1911:

> "Any person, firm, corporation or association who, with intent to sell or in any wise dispose of merchandise, securities, service, or

anything offered by such person, firm, corporation or association, directly or indirectly, to the public for sale or distribution, or with intent to increase the consumption thereof, or to induce the public in any manner to enter into any obligation relating thereto, or to acquire title thereto, or an interest therein, makes, publishes, disseminates, circulates, or places before the public, or causes, directly or indirectly, to be made, published, disseminated, circulated, or placed before the public, in this State, in a newspaper or other publication, or in the form of a book, notice, handbill, poster, bill, circular, pamphlet, or letter, or in any other way, an advertisement of any sort regarding merchandise, securities, service, or anything so offered to the public, which advertisement contains any assertion, representation or statement of fact which is untrue, deceptive or misleading, shall be guilty of a misdemeanor."

In the intervening years 42 states enacted laws regulating advertising based on *Printers' Ink* statute. Of that number 24 passed the law as quoted above in unamended form.[1] The statute was enacted by 18 other states but only after it had been weakened by inserting the word "knowingly" in such a way as to make it difficult to enforce the law.[2] The remaining six states—Arkansas, Delaware, Georgia, Maine, Mississippi, and New Mexico—had no general law governing advertising practices.[3]

A serious weakness is the inability of states to control interstate advertising. An increasingly large part of advertising is on a national scale, which means that individual states have no power of regulation. Magazines having a national circulation are subject only to control of Congress, since their distribution involves interstate commerce. Likewise radio broadcasting programs are under the control of the Federal Communications Commission.

The Lack of Federal Control. In the face of a growing need for control of interstate advertising, Congress did nothing effective until 1938. Until that year there was no general Federal statute regulating advertising practices. It is true that the Food and Drug Administration, the Postmaster General, and the Federal Alcohol Administration exercised some control but it was definitely limited. The power of the Food and Drug Administration did not go beyond the statements on labels; the

[1] They are Colorado, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Michigan, Minnesota, Missouri, Nebraska, Nevada, New Jersey, New York, North Dakota, Ohio, Oklahoma, Oregon, Rhode Island, Virginia, Washington, Wisconsin, Wyoming.

[2] These states are: Alabama, Arizona, California, Connecticut, Florida, Maryland, Massachusetts, Montana, New Hampshire, North Carolina, Pennsylvania, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, West Virginia.

[3] Gordon, Leland J., *Directory of Governmental Consumer Services and Agencies*, Bulletin No. 3, Consumer Division, National Defense Commission, pp. 13–14.

Office of the Solicitor in the Post Office Department has long guarded consumers against the use of the United States mails for the perpetration of fraud, for the conduct of lotteries, or for the transmission of indecent publications; the Alcohol Tax Unit of the Bureau of Internal Revenue co-operates with state agencies to regulate liquor in consumers' interests, with particular reference to labeling and advertising.[1]

Under provisions of the original Federal Trade Commission Act its primary purpose was to prevent unfair competition among competitors in interstate commerce. It proved practically impossible to regulate advertising on such a basis. Even if it were possible it would have been of little help to consumers, for the ultimate test was whether the advertising was unfair to competing businessmen rather than whether it was unfair to consumers.

In *Silver* vs. *Federal Trade Commission* in 1923 the court ruled that the Commission was created primarily to enforce antitrust and antimonopoly laws.[2] In *Raladam Company* vs. *Federal Trade Commission*, the power of the Commission was further restricted by the decision that advertisements of Marmola tablets, an obesity cure, alleged by the Commission to be so dangerous that it should be taken only under medical supervision, were not false or misleading since the statements were ones of opinion rather than fact.[3] This represents a renewal and extension of the common-law doctrine that a seller is not responsible for exaggerated statements concerning his product. Courts call this trade puffing and cling to the legal view that buyers ought to beware. This doctrine is doubly convenient for advertisers since it ignores inability of consumers to distinguish between truth and falsity in advertising.

Out of twenty-nine Federal Trade Commission orders dealing with false advertising which had gotten into the courts by 1938, twenty-two were upheld and seven were reversed. Among those sustained, the Royal Baking Powder Company was ordered to desist from advertising a phosphate baking powder as containing cream of tartar.[4] Procter and Gamble were ordered to desist from advertising the presence of naphtha in soap since by its very nature it is almost entirely evaporated by the time the soap reaches consumers.[5] Other cases forbade the misuse of such terms as mahogany, leather, satin, silk, shellac, and grape.

One case definitely involving false advertising and misbranding to reach the United States Supreme Court was that of *Federal Trade Com-*

[1] *Ibid.*, pp. 14, 28, 29.

[2] Federal Trade Commission, *Decisions*, vol. 6, pp. 559–574.

[3] *Ibid.*, vol. 14, pp. 683–694; vol. 15, pp. 598–606.

[4] *Ibid.*, vol. 4, pp. 614–625; vol. 11, pp. 677–691; pp. 701–704; vol. 12, pp. 740–742.

[5] *Ibid.*, vol. 10, pp. 661–664.

mission vs. *Winsted Hosiery Company* in 1922.[1] This company was charged with advertising underwear containing as little as 10 per cent virgin wool as "Natural Merino," "Grey Wool," "Natural Worsted," or "Australian Wool." The court upheld the Commission, holding that such statements must be accompanied by supplementary statements showing what other materials were used.[2] Even here, it will be noticed, there is no requirement that the actual percentage of wool be revealed. This emphasizes the fact that such authority as the Commission formerly possessed was designed solely for protection of competing producers rather than to aid consumers. As long as that situation persisted consumers had no effective protection from false advertising.

Beginning in 1934 the New Deal administration set out to remedy this weakness in Federal control. There had been a growing conviction in Congress that advertising should be regulated, but the central problem proved to be whether such effective control should be vested in the Federal Trade Commission or transferred to another branch of the government.

S2800, "a bill to prevent manufacture, shipment, and sale of adulterated or misbranded food, drink, drugs, and cosmetics, and to regulate traffic therein; to prevent the false advertisement of food, drink, drugs, and cosmetics; and for other purposes," was introduced into the Senate in the second session of the 73d Congress in 1934. Section 9 provided that

> "(*a*) An advertisement of a food, drug, or cosmetic shall be deemed to be false if it is false or misleading in any particular relevant to the purposes of this Act regarding such food, drug, or cosmetic. Any representation concerning any effect of a drug shall be deemed to be false under this paragraph if that representation is not supported by substantial medical opinion or by demonstrable scientific facts.
>
> "(*b*) An advertisement of a drug shall also be deemed to be false if it contains the name of any disease for which the drug is not a specific cure but is a palliative and fails to contain a plain and conspicuous statement, so placed as to be readily observable where such name occurs, indicating that the drug is a palliative and the nature of its palliative action."

The following section was stricken out in committee:

> "(*c*) To discourage the public advertisement for sale in interstate commerce of drugs for diseases wherein self medication may be especially dangerous, or patently contrary to the interests of public health, any advertisement of a drug representing it to have

[1] *Ibid.*, vol. 3, pp. 618–621; vol. 4, pp. 610–614.
[2] See also Handler, *op. cit.*, pp. 527, 539, 543.

any effect in the treatment of any of the following diseases shall be deemed to be false: Albuminuria, appendicitis, arteriosclerosis, blood poison, bone diseases, cancer, carbuncle, cataract, cholecystitis, dental caries or erosion, diabetes, diphtheria, dropsy, encephalitis, epilepsy, erysipelas, gallstones, goiter, heart diseases, high blood pressure, mastoiditis, measles, meningitis, mumps, nephritis, otitis media, paralysis, periodontal diseases, pneumonia, poliomyelitis, prostate gland disorders, pyelitis, scarlet fever, sexual impotence, sinus infections, smallpox, tuberculosis, tumors, typhoid, uremia, venereal diseases, and whooping cough; except that no advertisement not in violation of paragraph (*a*) or (*b*) of this section shall be deemed to be false under this paragraph if it is disseminated to members of the medical and pharmaceutical professions only or appears in the scientific periodicals of these professions, or if it is disseminated for the purpose of public health education by persons not commercially interested, directly or indirectly, in the sale of such drugs: *Provided*, That whenever the Secretary determines that an advance in medical science has made any type of self medication safe as to any of the diseases enumerated above, he shall promulgate regulations, as provided by section 22, exempting the advertisement of drugs having curative or therapeutic effect for such disease from the operation of this paragraph, subject to such conditions and restrictions as may be necessary in the interests of public health."

The bill was referred to the Committee on Commerce, which held hearings from February 27 to March 3, 1934. Tremendous opposition developed. One of the most common points of attack was the provision that the Secretary of Agriculture should have complete power to enforce the act.

The bill failed of passage, but substantially the same bill was introduced as S5 in the first session of the 74th Congress. Section 601 read,

"(*a*) An advertisement of a food, drug, or cosmetic shall be deemed to be false if it is false or misleading in any particular relevant to the purposes of this Act regarding such food, drug, or cosmetic. Any representation concerning any effect of a drug shall be deemed to be false under this paragraph if such representation is not sustained by demonstrable scientific facts or substantial *and reliable*[1] medical opinion.

"(*b*) For the purposes of this Act the advertisement of a drug representing it to have any therapeutic effect in the treatment of Bright's disease, cancer, tuberculosis, poliomyelitis (infantile paralysis), venereal diseases, heart and vascular diseases shall be deemed to be false; except that no advertisement not in violation of para-

[1] Italics supplied to call attention to significant qualifying words not found in paragraph (*a*) on page 190.

graph (*a*) of this section shall be deemed to be false under this paragraph if it is disseminated only to members of the medical and pharmaceutical professions or appears only in the scientific periodicals of these professions, or is disseminated only for the purpose of public-health education by persons not commercially interested, directly or indirectly, in the sale of such drugs."

Careful reading and comparison reveals the manner in which a bill whose passage is regarded as likely is weakened in the legislative process. Not satisfied with deleting section 9 (*c*), opponents so rewrote section (*b*) as to weaken still more its protective power for consumers. S5 also was referred to the Committee on Commerce, which held hearings March 2, 8, and 9, 1935. The bill was reported favorably and passed by the Senate. In the legislative jam which developed in the summer of 1935 the bill was never reported out by the House Committee to which it was referred.

By that time a sharp cleavage had developed between the two Federal legislative houses. The Senate held to the view that advertising control should be vested in the Food and Drug Administration, while the House insisted that the Federal Trade Commission was the proper administrative body. House Committee members argued that the broader aspects of advertising control reach far beyond food and drugs with which the Food and Drug Administration is primarily concerned and whose control facilities consequently would be inadequate. Senate Committee members insisted that the enforcement machinery of the Food and Drug Administration could be expanded logically and easily to include all advertising control; that advertising control is so closely related to administration and enforcement of the Pure Food and Drugs Act that more effective results might be obtained by concentrating the tasks than by dividing them between two separate bodies. Coloring the controversy were sharply different opinions concerning the relative merits of the two bodies. While Consumers' Research took the position that neither commission could be effective because both were too friendly to the business groups supposedly subject to control, members of Congress and of the Administration were inclined to favor one of the two bodies over the other. Outside of government, friends of advertising control generally inclined toward the Food and Drug Administration, while opponents, including advertisers, strongly favored the Federal Trade Commission.

A leader of the House group demanding Federal Trade Commission control of advertising was Representative Clarence Lea, who introduced and sponsored an amendment to the original Federal Trade Commission Act, granting control powers to the Commission. While the House insisted on passage of its bill or none, the Senate was equally insistent that

control be vested in the Food and Drug Administration. That impasse continued for four years. It was broken in the winter of 1938, when the Senate finally acceded to the House view and the following sections were added to the Federal Trade Commission Act.

"Sec. 12. (*a*) It shall be unlawful for any person, partnership, or corporation to disseminate, or cause to be disseminated, any false advertisement—

"(1) By United States mails, or in commerce by any means, for the purpose of inducing, or which is likely to induce, directly or indirectly the purchase of food, drugs, devices, or cosmetics; or

"(2) By any means, for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase in commerce of food, drugs, devices, or cosmetics.

"(*b*) The dissemination or the causing to be disseminated of any false advertisement within the provisions of subsection (*a*) of this section shall be an unfair or deceptive act or practice in commerce within the meaning of section 5.

"Sec. 13. (*a*) Whenever the Commission has reason to believe—

"(1) that any person, partnership, or corporation is engaged in, or is about to engage in, the dissemination or the causing of the dissemination of any advertisement in violation of section 12, and

"(2) that the enjoining thereof pending the issuance of a complaint by the Commission under section 5, and until such complaint is dismissed by the Commission or set aside by the court on review, or the order of the Commission to cease and desist made thereon has become final within the meaning of section 5, would be to the interest of the public,

the Commission by any of its attorneys designated by it for such purpose may bring suit in a district court of the United States or in the United States court of any Territory, to enjoin the dissemination or the causing of the dissemination of such advertisement. Upon proper showing a temporary injunction or restraining order shall be granted without bond. Any such suit shall be brought in the district in which such person, partnership, or corporation resides or transacts business.

"(*b*) Whenever it appears to the satisfaction of the court in the case of a newspaper, magazine, periodical, or other publication, published at regular intervals—

"(1) that restraining the dissemination of a false advertisement in any particular issue of such publication would delay the delivery of such issue after the regular time therefor, and

"(2) that such delay would be due to the method by which the manufacture and distribution of such publication is customarily conducted by the publisher in accordance with sound business practice, and not to any method or device adopted for the evasion of this section

or to prevent or delay the issuance of an injunction or restraining order with respect to such false advertisement or any other advertisement, the court shall exclude such issue from the operation of the restraining order or injunction.

"Sec. 14. (*a*) Any person, partnership, or corporation who violates any provision of section 12 (*a*) shall, if the use of the commodity advertised may be injurious to health because of results from such use under the conditions prescribed in the advertisement thereof, or under such conditions as are customary or usual, *or if such violation is with intent to defraud or mislead*,[1] be guilty of a misdemeanor, and upon conviction shall be punished by a fine of not more than $5,000 or by imprisonment for not more than six months, or by both such fine and imprisonment; except that if the conviction is for a violation committed after a first conviction of such person, partnership, or corporation, for any violation of such section, punishment shall be by a fine of not more than $10,000 or by imprisonment for not more than one year, or by both such fine and imprisonment: *Provided*, That for the purposes of this section meats and meat food products duly inspected, marked, and labeled in accordance with rules and regulations issued under the Meat Inspection Act approved March 4, 1907, as amended, shall be conclusively presumed not injurious to health at the time the same leave official 'establishments.'

"(*b*) No publisher, radio-broadcast licensee, or agency or medium for the dissemination of advertising, except the manufacturer, packer, distributor, or seller of the commodity to which the false advertisement relates, shall be liable under this section by reason of the dissemination by him of any false advertisement, unless he has refused, on the request of the Commission, to furnish the Commission the name and post-office address of the manufacturer, packer, distributor, seller, or advertising agency, residing in the United States, who caused him to disseminate such advertisement. No advertising agency shall be liable under this section by reason of the causing by it of the dissemination of any false advertisement, unless it has refused, on the request of the Commission, to furnish the Commission the name and post-office address of the manufacturer, packer, distributor, or seller, residing in the United States, who caused it to cause the dissemination of such advertisement.

"Sec. 15. For the purposes of sections 12, 13, and 14—

"(*a*) The term 'false advertisement' means an advertisement, other than labeling, which is misleading in a material respect; and in determining whether any advertisement is misleading there shall be taken into account (among other things) not only representations made or suggested by statement, word, design, device, sound, or any combination thereof, but also the extent to which the advertisement fails to reveal facts material in the light of such representations or material with respect to consequences which may result from the use of the commodity to

[1] Italics supplied.

which the advertisement relates under the conditions prescribed in said advertisement, or under such conditions as are customary or usual. No advertisement of a drug shall be deemed to be false if it is disseminated only to members of the medical profession, contains no false representation of a material fact, and includes, or is accompanied in each instance by truthful disclosure of the formula showing quantitatively each ingredient of such drug.

"(*b*) The term 'food' means (1) articles used for food or drink for man or other animals, (2) chewing gum, and (3) articles used for components of any such article.

"(*c*) The term 'drug' means (1) articles recognized in the official United States Pharmacopœia, official Homœopathic Pharmacopœia of the United States, or official National Formulary, or any supplement to any of them; and (2) articles intended for use in the diagnosis, cure, mitigation, treatment, or prevention of disease in man or other animals; and (3) articles (other than food) intended to affect the structure or any function of the body of man or other animals; and (4) articles intended for use as a component of any article specified in clause (1), (2), or (3); but does not include devices or their components, parts, or accessories.

"(*d*) The term 'device' (except when used in subsection (*a*) of this section) means instruments, apparatus, and contrivances, including their parts and accessories, intended (1) for use in the diagnosis, cure, mitigation, treatment, or prevention of disease in man or other animals; or (2) to affect the structure or any function of the body of man or other animals.

"(*e*) The term 'cosmetic' means (1) articles to be rubbed, poured, sprinkled, or sprayed on, introduced into, or otherwise applied to the human body or any part thereof intended for cleansing, beautifying, promoting attractiveness, or altering the appearance, and (2) articles intended for use as a component of any such article; except that such term shall not include soap.

"Sec. 16. Whenever the Federal Trade Commission has reason to believe that any person, partnership, or corporation is liable to a penalty under section 14 or under subsection (1) of section 5, it shall certify the facts to the Attorney General, whose duty it shall be to cause appropriate proceedings to be brought for the enforcement of the provisions of such section or subsection."

The staff of the Radio and Periodical Division of the Federal Trade Commission examined over one million advertisements in a recent year. The media examined included five thousand pages of radio continuities daily, 533 magazines in the English language and two in foreign languages, 463 newspapers in English, and 25 newspapers printed in European languages. In addition there is a regular survey of mail-order catalogs and circulars of 68 firms, which amounts to twenty thousand

pages of mail-order advertising. It should be made clear, however, that the examination of one million separate advertisements does not mean nor imply that they cover one million different products or one million different claims. The annual report indicates that the questioned advertisements concerned 2839 commodities.

Out of the total number of advertisements reviewed monthly those which are likely to develop into cases are assembled for further investigation. In February, 1942, the number marked for further investigation was 283. Enforcement procedure for these cases follows the established Federal Trade Commission pattern. Any perpetrator of false advertising is served with a complaint, being given opportunity to appear for a hearing and to show cause why a cease-and-desist order should not be issued. If the hearing yields no significant new evidence the Commission issues a formal order to cease and desist from using such false advertising. Provision for court review is granted. As a matter of practice the Commission seeks to use an informal method resulting in voluntary discontinuance of illegal practices. Thus the automobile finance affiliates agreed to cease advertising the "6 per cent plan" of installment credit because the Commission contended that such a plan actually resulted in a much higher rate and consequently the advertising was false and misleading. Toward that end the Commission works with trade associations, urging them to set up their own rules of fair trade practice. As an illustration the National Retail Dry Goods Association and the Toilet Goods Association worked out a plan under which all advertising claims are approved by the board of standards of the Toilet Goods Association, or any competent independent laboratory.

In February 1944 a bill was introduced in Congress empowering the Federal Trade Commission to require advertisers who have been making false claims for their products to inform the public of their misdeeds through publication of the Commission's orders. It was contemplated in the bill that the Commission could require the offending advertiser to give at least as much periodical space or radio time to the contents of the Commission order as it had previously given to the original advertisement.

Earlier in this chapter reference was made to several Federal Trade Commission decisions and stipulations pertaining to false and misleading advertising. There can be no doubt that the general level of advertising has improved. There is no way of knowing whether the Federal Trade Commission has done as good a job as, or a better job than, the Food and Drug Administration would have done. Among the advertising and trade journals there is a very definite feeling that the Federal Trade Commission has been much "tougher" than was expected. This feeling is

particularly acute in the proprietary drug trade. According to *Business Week* the Federal Trade Commission was formerly the industry's favorite government regulatory agency, but now the authority of the Commission is being challenged in court by this industry and it was reported that an effort was made to curtail its activities by limiting its appropriation. "For years, FTC has been a favorite with Congressmen—it has never caused trouble or fuss like agencies such as the Federal Communications Commission or the National Labor Relations Board. Generally, appropriation bills containing FTC funds were rushed through. This year, however, when FTC appeared before the routine secret session of the House subcommittee on appropriations to support its request for funds, it was surprised to find Everett Dirksen (R., Ill.) primed with questions as to its methods of operating in the drug field. Later, when FTC appeared before a similar Senate subcommittee, Styles Bridges (R., N. H.), assisted by Clyde M. Reed (R., Kan.), directed sharp cross examination at Commission officials."[1]

On the other hand it was reported at about the same time that Congressman John M. Coffee of Washington was considering the introduction of a resolution for a Congressional investigation to discover why the Commission had not enforced more vigorously the Wheeler-Lea Amendment to the Federal Trade Commission Act. He wanted to know particularly why the Commission had not used the injunction power nor the criminal penalty for advertising food, drugs, and cosmetics with results that may be injurious to health. It was alleged that the Commission had picked on a few small firms but had ignored some of the large firm offenders.[2]

Social Balance Sheet of Advertising

Conflicting Points of View. It is a persistent fact that economic interests of individuals and groups conflict. This is effectively demonstrated by advertising. What is a good advertisement? The standards by which a commercial artist judges are line and color, while to a printer they are type and format; the standard for a lithographer is color, while that for the psychologist is appeal; a publisher judges an advertisement by its size, while the one who pays the bill judges its effectiveness by results. Consumers alone are without definite objective tests by which to measure advertising effectiveness. Critical consumers judge advertisements by reliable information presented and find far too many of them deficient. It has been shown that in modern economic organization advertising has a definite place and a function to perform. As it is used, however,

[1] *Business Week,* May 29, 1943. [2] *Business Week,* April 15, 1939. For further discussion of advertising control see Chapter 28.

producers' interest in profit predominates over consumers' interest in service. From a consumer point of view the problem is to eliminate waste by restricting advertising to its economic functions. While Federal law can help to achieve this objective, the final responsibility rests with consumers themselves. As long as they permit themselves to be manipulated like marionettes it will pay producers to continue prevailing advertising practice. It will be difficult to enact legislation which unscrupulous advertisers cannot circumvent. When such advertisers find that false and misleading advertising no longer pays, then, and only then, will they adhere to truth in advertising. The solution of the problem therefore rests with consumers. If and when they demand truthful, informational advertising they will get it. While this implies that we may some day have truthful and useful advertising, it is doubtful whether these results can be achieved in a pecuniary society. Consumers as consumers are too ignorant and will continue to be so as long as producers can retain control of important channels of information. Custom operates effectively to maintain this unbalanced power. It must be concluded, therefore, that by means of high-pressure salesmanship and advertising, producers influence powerfully the nature of consumers' economic choice. More than a majority of consumers are influenced if they are not almost completely controlled by producers. To the extent that this is true their area of free choice is seriously and significantly restricted.

Summary

Intelligent consumers are more concerned with what advertising actually does than with what it might do. Critical analysis shows that some advertising is wasteful because it is misdirected; much of it is quite useless as a source of information and is wasteful because of its competitive nature; some advertising is deceptive and is wasted because it is devoted to nealth and illth and tends to stimulate artificial consuming practices; from a social viewpoint advertising actually decreases production of wealth, at the same time misusing art and science. Psychology particularly has been perverted to unsocial purposes. The advertising agency operates inefficiently and wastefully. In their determination to get results some advertisers have practically ignored all ethical standards. Conditions became intolerable by 1910 and led to efforts by legitimate and ethically minded persons in the business to set up machinery for control. State laws have been enacted but the problem is largely interstate and the Federal government has only recently enacted regulative legislation. This illustrates clearly the basic conflict between individual and group point of view and leads to the conclusion that effective control of undesirable advertising and elimination of unnecessary advertising cannot

be secured by laws. Final and direct responsibility rests with consumers. As long as they make it profitable for producers to adhere to current advertising practices by allowing themselves to be influenced, producers will continue to spend hundreds of millions of dollars annually appealing to emotions. When consumers demand honest, informative advertising they will get it. But will they demand it?

QUESTIONS FOR DISCUSSION

1. Can you suggest any additional criticisms of current advertising practices?
2. Do you think all the criticisms in the text are valid?
3. Give an illustration of competitive advertising, based on your own observation.
4. What consumer purpose is served by advertising salt? Gasoline?
5. Would you favor a national advertising campaign for X brand of matches?
6. Has your experience with advertising engendered confidence in its reliability?
7. What do you think an advertiser regards as your proper function?
8. Are consumers performing a social service when they discard goods still possessing use value?
9. Why, do you think, are the movies less given to advertising than the radio?
10. Have you ever switched cigarettes or dentifrices as a result of competitive advertising?
11. Is the contention that advertising decreases production valid?
12. What do you think is the effect of advertising on art? On science?
13. In contrast to a psychology for advertisers can you outline a psychology for consumers?
14. Try expanding your psychology for consumers to include a contrast with psychology for salesmen.
15. Do you think advertisers themselves might control advertising practices effectively?
16. Have you ever reported an advertising fraud to your local Better Business Bureau?
17. Do you think the Federal Trade Commission is the proper body to regulate interstate advertising?

PROBLEMS AND PROJECTS

1. Submit six advertisements taken from current periodicals or newspapers which fail to meet the standard you set up for Project 1 in Chapter 10 (page 166). Indicate whether each advertisement is false, misleading, or neutral; compare advertisers' claims with Consumers Union or Consumers' Research Reports on the advertised articles.

2. Set up a standard of advertising appeals to college men and women and rate the more common broadcasting programs or the current issue of a magazine like the *Saturday Evening Post* or *Life*.

3. Analyze and classify the advertisements in a typical magazine among truthful, doubtful, misleading, deceptive.

4. Count the number of advertisements in a magazine like *Good Housekeeping* making use of science in some way.

5. Classify the psychological appeals used and record the number of times they occur in a current popular magazine.

6. Visit a large city advertising agency; secure all the information you can as to organization and methods.

7. If you live in or near a large city visit the Better Business Bureau and write a report on its activities and effectiveness.

8. Is the model law to regulate advertising sponsored by *Printers' Ink* in force in your state? If so, give its provisions and ascertain how effectively it is enforced. If you have no state law regulating advertising, why has none been enacted?

9. Examine reports of the Federal Trade Commission and summarize actions dealing with advertising during the past year.

10. Review Rorty, James, *Advertising: Our Master's Voice*, or Woodward, Helen, *Through Many Windows;* or Hower, Ralph M., *The History of an Advertising Agency*.

12

The Profitable Practice of Fraud

What Is Fraud?

Let the Buyer Beware. In an economic system organized on the assumption that every individual will seek to promote his self-interest by acquiring for himself as much profit as possible, it is an easy step to the practice of attempting to secure profit by any possible means. From an individual point of view it makes no difference whether profit accrues from the rendering of a service or from a disservice. So regarded, resort to gambling, fraud, swindling, or even outright theft is simply the logical outcome of the operation of self-interest and the profit motive.

Traditional economic theory holds that consumers are protected from such practices by the force of competition. Entering the market place in search of goods with which to satisfy their wants, consumers are supposed to act as economic men. This means that they will shop at all places where goods are for sale, comparing prices and quality, and that final purchase will be made at the store offering the highest quality at the lowest price. If by any chance this assumed economic man should make a mistake, theory holds that he will refuse to patronize the same merchant again, and will find the right store instead. This theory is based on assumptions that consumers act as economic men and that mistakes will be discovered. In practice consumers are not economic men, and as a result competition fails to operate as a protective device. Even if competition did operate there are times when mistaken purchases result in death—and there can be no compensating change to another store—or in illness or delusion created by heavily drugged preparations. This latter condition helps to explain many testimonials written by persons who were sincere in their belief that they were improved but who, in fact, have died within a few weeks or months after their supposed cure.

Let the buyer beware! This has become the slogan of the market place. Indeed the buyer needs to be wary. Out of the billions of dollars' worth of goods annually produced and counted as wealth a large portion consists of nealth or illth. Such things are perhaps the source of wealth to those who produce them, but they are not wealth to consumers in the sense of promoting their welfare.

Large-Scale Fraud. In colonial days when productive processes were

simple and the number of consumers comparatively small it was much more difficult to perpetrate fraud. By the very nature of the system in which they lived, colonial consumers were better equipped to play the part of wary consumers in a competitive market. Small-scale producers necessarily dealt largely with people who were their neighbors, so it was much more difficult for them to cheat their customers even if they were so disposed.

Since that time relations between producers and consumers have undergone very great change. Modern fraud is not only impersonal but is perpetrated on a grand scale. Modern conditions ease the consciences of fraudulent practitioners. With but few exceptions, the impersonality of the modern market frees them from the necessity of facing their victims. To the dealer in fraud every consumer is a possible victim. In a market of 136,000,000 potential buyers there need be no concern for repeat sales. Once the market has been exhausted some new trick or device offered under a new corporate name holds all the possibilities of a fresh start. Thus one man was reported to have made as much as $600,000 a year marketing a dangerous drug advertised as a fat reducer. During his colorful career he operated, from time to time, under four different company names.[1]

Not All That Deceives Is Fraudulent. If fraud is dishonest and works to consumers' illfare why is it not declared illegal and prevented? In a broad sense this is what has been done, but some things that deceive are not fraudulent, legally. Just what does constitute fraud is a matter of definition. If it were defined in law as it is in the dictionary, as any artifice by which the right or interest of another person is injured, consumers would have much more protection and fraudulent producers much less. Actually, laws and courts have so defined and limited the meaning of fraud as to restrict it to deliberate deceit. This means that in a court case the plaintiff must prove that the intent of the seller was to deceive the buyer. This is extremely difficult to do. As a result, salesmen of much merchandise that actually does deceive consumers are protected by the leniency of the laws.

This situation is aggravated by the freedom of any person to go into almost any business he chooses. In some cases the law recognizes the need for protecting consumers from fraudulent practitioners. This is the basis for requiring licenses to practice medicine or to compound drugs. Yet a man without the slightest training in medicine or chemistry may set himself up as a company for producing some marvelous cure. Direct damage suits by injured consumers are comparatively uncommon, while

[1] Lamb, Ruth de Forest, *American Chamber of Horrors*, pp. 5–9, Farrar & Rinehart, New York, 1936.

state and Federal laws are quite inadequate to protect consumers.[1] This situation supplies protection for the individual in his acquisitive actions, but as a consumer it leaves him a victim of his own weakness.

Fields of Fraud

Every Human Want. The entire range of human wants presents opportunities for fraud. Basic wants for food and clothing have long been cultivated. The more usual forms of fraud are adulteration, misbranding, misrepresentation, short-changing, short-measuring, and short-weighting. Here again consumer protection is handicapped by legalistic interpretations. Food adulteration, for example, is defined as adding any deleterious or harmful ingredient, although in fact it may result from the presence of some harmful ingredient inherent in the product.

Charlatans also cater to the human desire for health, wealth, and beauty. Even religion is subject to fraudulent practice. The various fields of fraud are too numerous to cover in a single chapter but the interested reader may turn to other books (listed at the foot of this page) which deal in detail with various aspects of fraud. The purpose of this discussion is to present selected evidences of fraud from the consumer rather than from the legal point of view, with the aims of developing wary consumers and demonstrating the need for better laws. Various books on the subject are of recent date.[2]

Evidences of Fraud

Food Frauds. In addition to adulteration, misbranding, misrepresentation, short-changing, short-measuring, and short-weighting, over-

[1] The nature and operation of Food and Drug Laws are discussed in Chapter 28.

[2] (1) Bender, Eric, *Tickets to Fortune*, Modern Age Books, New York, 1938. (2) Cramp, Arthur J., *Nostrums and Quackery*, vol. 1, 1911; vol. 2, 1921; vol. 3, 1936, American Medical Association, Chicago. (3) Harding, T. Swann, *The Popular Practice of Fraud*, Longmans, Green & Company, New York, 1935. (4) Kallet, Arthur, *Counterfeit*, The Vanguard Press, New York, 1935. (5) Kallet, Arthur, and Schlink, F. J., *100,000,000 Guinea Pigs*, The Vanguard Press, New York, 1933. (6) Lamb, Ruth de Forest, *American Chamber of Horrors*, Farrar & Rinehart, New York, 1936. (7) Malmberg, Carl, *Diet and Die*, Hillman-Curl, Inc., New York, 1935. (8) Palmer, Bissell B., *Paying Through the Teeth*, The Vanguard Press, New York, 1935. (9) Phillips, M. C., *Skin Deep*, The Vanguard Press, New York, 1934. (10) Schlink, F. J., *Eat, Drink and Be Wary*, Covici-Friede, New York, 1935. (11) Riis, Roger W., and Patric, John, *Repairmen Will Get You If You Don't Watch Out*, Doubleday, Doran & Co., Garden City, New York, 1942. (12) Solomon, Charles, *The Traffic in Health*, Navarre Publishing Co., New York, 1937. (13) Baarslag, Karl, *Robbery By Mail*, Farrar & Rinehart, New York, 1938.

The field of fraud has assumed such proportions that there is now published bimonthly a magazine the title of which is *Frauds and Answers*. It is published at La Crescenta, California, and the subscription price is 25 cents a copy or $2 for two years. A brief story describing the magazine and the editor will be found in *Tide*, July 15, 1943.

pricing should be included as a fraud. Even though food may be pure, properly branded, and honestly weighted, consumers are deceived if they think they are getting overpriced merchandise at a fair price. Food poisoning is commonly, though not necessarily, associated with food frauds. Scientific data concerning food poisoning are still meager; but a popular tendency is to blame ptomaine poisoning, canned goods, or bad combinations. There is usually more fraud in selling food in periods of depression than in normal times. This is to be explained by the insistence of consumers on low-priced foods, and the practice of producers attempting to meet that demand by using cheap ingredients or substitutes. Modern production methods have led to the discovery of numerous synthetic substitutes. The use of glucose prepared by the aid of sulphuric acid may cause arsenical poisoning. Foods wrapped in tinfoil, bottled drinks capped with metal stoppers, and lead chromate used for yellow color may cause lead poisoning. Similarly, the use of aniline dyes for artificial coloring may poison consumers. Whether injurious or not, bleached flour, stained butter, and dyed jelly are certainly less desirable than the unaltered products. The shifting of canning and preserving from home to factory has led to emphasis on profit instead of family welfare. Such artificial, dangerous preservatives as formaldehyde, sulphite, and salicylic and sulphuric acids are effective in preserving food because of their poisonous effect on bacteria; but they have the same effect on human protoplasm.[1]

The consumers' usual guide for determining the quality of fresh fruit and vegetables is color. Producers have capitalized on this fact by developing methods of coloring fruit artificially. By using ethylene gas the green color in a fruit skin is destroyed, permitting the previously concealed red or yellow to show. If too much gas is used the fruit is burned, producing brown spots such as are sometimes seen on grapefruit or oranges. If the air is not sufficiently damp during the coloring process the fruit shrivels, while too high temperature partially cooks the fruit. Certain fruits can be treated so as to improve their appearance without injury, but in some cases the quality is affected and the fruit rendered definitely undesirable.

Use of ethylene gas to deceive consumers has led producers increasingly to adopt the practice of adding color to their fruit. Although the color of an orange bears no necessary relation to its quality, color is the basis on which most women buy. Inferior oranges if richly colored will sell better than superior oranges with skins that are yellow. The ethylene process often leaves oranges a sickly yellow. That defect is

[1] JORDAN, Edwin Oakes, *Food Poisoning*, University of Chicago Press, Chicago, 1917.

overcome by simply adding aniline dye. If every orange is stamped to show that color has been added, and unless it can be proved definitely that the coloring process is injurious to consumers or conceals inferiority, the law holds that no fraud has been perpetrated. Artificial colors may be used legally for cake frostings and candies. If, however, color is added to a product so as to give the impression that it contains certain fruit juices such practice is held fraudulent unless declared on the label. Real maraschino cherries are naturally flavored cherries packed with alcoholic cordial. Careful reading of the label on a bottle of so-called maraschino cherries may show clearly that the product is artificially flavored, artificially colored, and artificially preserved with benzoate of soda; and probably those so-called maraschino cherries were originally white fruit preserved in brine, treated with sulphurous acid, dyed with artificial red color, and flavored with benzaldehyde. Consumers who want assurance that food dyes they purchase are safe should look for the manufacturer's certification that his colors meet Federal specifications for purity.[1]

A summary of actions taken by the Food and Drug Administration as revealed in *Notices of Judgment* gives a fair indication of the variety of food frauds. Of 200 cases publicized in a typical period 16 involved adulteration of cereal and bakery products, 38 dealt with adulteration of butter and cheese, 16 cases involved fisheries products which were adulterated, many of the shipments consisting of products which consisted in whole or in part of a decomposed substance; there were 50 cases dealing with adulterated or misbranded fruits and vegetables, substitution being one of the common forms of adulteration; 8 cases of adulterated poultry were reported, the adulteration taking the form largely of shipping diseased or decomposed animals; 8 of the cases concerned nuts and nut products, the most common charge being that they contained or consisted of a filthy substance; 24 cases involved the adulteration of candy, many of the shipments being found to consist in whole or in part of a filthy substance, such as fragments of insects and rodent hairs.[2] Many consumers like to think that such actions on the part of the Food and Drug Administration are directed chiefly against unknown, irresponsible producers. To such people it must be disconcerting to learn that a very large corporation which puts out a popular and well-known line of canned products has been involved in 35 legal actions, while similarly well-known packers of meat products have been involved in 53 actions.

A few random illustrations will show the nature and variety of food

[1] *Consumers' Guide*, July 22, 1935; April 20, 1936.

[2] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act*, May, 1943, Cases 3651–3850.

adulteration in common practice. A large midwest milling company admitted the charge that an interstate shipment of flour was adulterated "in that it consisted in whole or in part of a filthy substance." The product was released under bond for denaturing under the supervision of the Food and Drug Administration and on condition that it be disposed of for purposes other than human consumption. Pleading guilty to a charge of an interstate shipment of butter containing less than the legal limit of butterfat, a midwest creamery was fined $25 and costs. Admitting that it had shipped across state lines 225 boxes of cheese which was adulterated "in that it consisted in whole or in part of a filthy substance and was otherwise unfit for food; and that it had been prepared, packed or held under insanitary conditions whereby it might have been contaminated with filth," a southern dairy product firm was permitted to reclaim the product under bond for use as hog feed. One shipper of oysters whose products contained added water failed to appear, so the shipment was destroyed. Another oyster firm, admitting that its product was adulterated, "in that it consisted in whole or in part of a decomposed substance," was permitted to recondition its product, separating the fit from the unfit portion and destroying the latter. Up in New England a food firm shipped 705 cases of tomato juice which was alleged to be adulterated in that it consisted in whole or in part of a filthy substance. No claimant appeared to claim the product, so it was destroyed.[1]

The following cases illustrate misbranding of products. A shipment of 96 cases of chicken-noodle dinner was seized at Cincinnati, Ohio. The containers were labeled in part "Morton's Southern Style Chicken Noodle Dinner. Ingredients: Egg Noodles, Chicken Broth, Chicken, Mushrooms, Peppers, Spices, and Seasoning. All Meat Visible." The Food and Drug Administration contended that the product was misbranded since the name implied the presence of more than 7 per cent chicken meat, that the use of the word "Mushrooms" was false and misleading, implying the presence of more than one or two small mushroom pieces per jar; that the container was packed with the chicken meat facing the jar, thereby misleading a prospective buyer. The shipper admitted the allegations, whereupon a judgment of condemnation was entered and the product was ordered released under bond to be converted into soup, repackaged, and relabeled under the supervision of the Food and Drug Administration.

Large shipments of olive oil were seized at several points in Alabama, Pennsylvania, Wisconsin, and Louisiana on the charges of adulteration and misbranding. The labels indicated "Pure Imported Olive Oil" although the contents of the packages consisted of a mixture of olive oil

[1] *Notices of Judgment*, *op. cit.*, Cases 3656, 3690, 3703, 3720, 3722, 3760.

and cottonseed oil. This time no one claimed the shipment, whereupon a portion was distributed to charitable institutions, the remainder being destroyed.

A shipment of 76 dozen cartons of extract of vanilla was found to be misbranded because the bottle did not occupy more than 26.30 per cent of the capacity of the carton. It was held that the containers were so made, formed, or filled as to be misleading, and the shipper was permitted to repackage it in suitable and proper containers under the supervision of the Food and Drug Administration.

The final case to be cited arose out of a shipment of a product represented as an aid in weight control and as a tonic. A shipment of 480 cans of Betene was seized at Rochester, New York, on charge of misbranding. "Analysis of the article showed that it consisted essentially of a mixture of dried skim milk, dried egg yolk, soybean tissues, wheat bran, wheat germ, salt, agar agar, calcium phosphate, chondrus (Irish moss), and saccharin flavored with cocoa, vanillin, and coumarin, together with certain added vitamin substances." It was claimed on the label that when this preparation was consumed as directed it would "cause an increase in weight, would supply vigor and vitality to users," and that it constituted a sure, sane, safe, and effective way to reduce. Actually it would not accomplish any of those results. The shipper admitted all the charges, whereupon the product was released under bond for relabeling under the supervision of the Food and Drug Administration.[1]

Health for Sale. The yearning for good health is universal, but efforts to buy it in bottles provide a fertile field for quackery. The basis of good health is simple, nourishing food, outdoor exercise, and sufficient rest. The modern tempo of life interferes with simple living. Deficiency of the three fundamentals (food, exercise, and rest), together with germ diseases and the various adulterated foods consumed, may cause illness to replace wellness. Consumer welfare is thereby retarded.

One might expect that on losing their health consumers would turn to doctors of medicine or to doctors of osteopathy, but modern methods of providing such helpful services result in prices altogether too high for many people. It is largely among these that quack practitioners and compounders of cure-all remedies find their largest market. Persons in ill health, discouraged and dejected, read with wonder the glowing words of self-praise widely advertised by such men. In hopeful enthusiasm they will spend fifty cents or a dollar for a bottle or package in the belief that even if it does no good it will do no harm. The situation would be bad

[1] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act*, May, 1943, Cases 3666, 3675, 3715, 3742, 3801, 3843, 3840.

enough if that were true, but unfortunately some patent medicines are positively injurious.

As Dr. Cramp emphasizes in his discussion of *Nostrums and Quackery* (p. 203), nature is on the side of the quack. Probably 80 per cent of all human ills disappear whether the afflicted person resorts to medication or not. Many people take several doses of some harmless concoction, or some slightly harmful concoction, and regain their normal health in spite of it. Others afflicted with more serious diseases enjoy a temporary psychological relief. In either case they respond eagerly to the suggestion of writing a testimonial. This response may be superinduced by monetary reward, by the simple thrill of seeing one's name in print, or by a genuine belief in the curative powers of the medicine they recommend. In those cases where illness is really serious, resort to proprietary preparations is doubly dangerous, for they not only will probably fail to cure but will also cause the loss of valuable time in the final resort to approved methods of treatment.

Another force playing into the hands of quacks is the prevalent superstition concerning many cures. Social groups in primitive tribes have their medicine men and cults. Indeed many proprietary preparations are supposedly based on the magic healing powers of herbs or roots discovered by some tribal chieftain. The difficulty lies in the fact that there is sometimes sufficient basis in fact to lend credence to such beliefs. Dr. Walter C. Alvarez of the Mayo Clinic has written: "But someone may remind me that sometimes a quack *does* cure after able physicians have failed. And that is right; I have seen this myself; but no one who knows anything about quackery, or human suggestibility, or hysteria, or the tendency of most diseases to abate without treatment at all, is ever going to conclude that simply because a man is curing some people and is gathering crowds on his doorstep he is a good physician and his system of practice is worth investigating or imitating."[1] An old heathen custom was that of saving and drying placenta after childbirth; and in later years whenever the child was sickly the dried placenta was fed him as good medicine. Experiments by Dr. E. S. Robinson of the Massachusetts Department of Public Health and Dr. C. F. McKhann of the Harvard Medical College have demonstrated a high degree of success in using purified placental extract in the treatment of measles.[2] To a nostrum vendor it is not a long step from such scientific verification to the wholesale advertising of some weakened solution as a sure cure for all

[1] Reprinted by permission of Columbia University Press from Walter C. Alvarez, 'From Folkways to Modern Medicine," in Lectures to the Laity of the New York Academy of Medicine, *The March of Medicine* (1940).

[2] *New York Times*, October 11, 1935.

human ailments. Thus a certain patent medicine, consisting of a half cent's worth of cream of tartar in water, has been sold at the rate of $15 a pint as a cure for scarlet fever and smallpox.[1]

The following illustrations of adulterated drug preparations entering into interstate commerce will serve to indicate the extent of fraud in this field. An article consisting essentially of boric acid, zinc sulfate, and a small amount of flavoring oil was represented as an antiseptic powder. Not only was the article adulterated as a result of its inferior strength and purity but statements on the label were false and misleading. Instructions were to dissolve two level teaspoonfuls in a little boiling water and then add two quarts of lukewarm water. In that form it was to be used as a douche which would protect the user's health and produce curative and therapeutic effects. The manufacturing corporation pleaded guilty and the court imposed a fine of $150 on each of six counts, totaling $900.

Shipped from San Francisco to Seattle, portions of 122 five-gallon cans of Bonita livers were found to be decomposed and putrid. The claimant, a well-known drug firm, admitted the charge, whereupon the product was released under bond, conditional upon its being re-worked so as to comply with the law. All cans containing the product were inspected and those found to be unfit were destroyed.

Another well-known drug firm shipped 47 bags of ginger from New Jersey to Tennessee. Investigation disclosed the product to be adulterated in that it consisted in whole or in part of a filthy, putrid, or decomposed substance. The charges were admitted and the product was released for re-working under bond.

A shipment of aromatic spirits of ammonia was found to be adulterated in that the ammonia content in some instances exceeded the maximum and in other instances fell below the minimum prescribed in the United States Pharmacopoeia.

A product shipped from California to Oregon, purporting to be Vitamin A and D tablets, proved to be more than 50 per cent deficient in Vitamin A and more than 40 per cent deficient in Vitamin D.

A product labeled "Isopropyl Alcohol 25 per cent" was found to contain only 10 per cent by volume of Isopropyl Alcohol.

A shipment of capsules for the treatment of head colds was held to be potentially dangerous to health when used according to directions, since the capsules in the 25-cent-sized packages contained more acetanilid than the amount stated on the label, and those in the 50-cent-sized packages bore false and misleading therapeutic claims and failed to bear the required ingredient and quantity of content statement. In

[1] Kallet, Arthur, and Schlink, F. J., *100,000,000 Guinea Pigs*, p. 163.

both cases the labels failed to warn the users that their use might be dangerous to health, particularly in the presence of symptoms of appendicitis.[1]

Cases of fraud involving misbranding are even more numerous. Nature's Minerals Compound was held to be dangerous to health when used according to directions. Moreover, the labeling was held to be false and misleading. An accompanying circular pictured a hotel surrounded by palm trees, and the copy clearly implied that the article could be used in place of spending $200 to $300 a month at a health resort. The product was represented as being helpful in the treatment and alleviation of conditions for which a sojourn at a health resort is customarily prescribed. The labeling implied that the product would restore health and prevent weakness, that the Compound was necessary to render the blood stream alkaline, that it would correct the causes of flabby tissues and the effects of faulty elimination, that it would insure the user that he would live to an advanced age without feeling old or losing his capacity to think or work, that it was necessary for the proper functioning of important body processes, and so on through many additional claims. The defendants pleaded guilty and were fined $200.

There were several fraudulent aspects of a shipment of cold tablets from Michigan to Washington. The labels failed to bear adequate warning statements; they carried false and misleading statements regarding therapeutic value; false statements concerning the amount of acetanilid contained in the tablets; and finally the packages were deceptive since 30 per cent of the upper space in the carton was empty. Analysis of the tablets showed that they consisted essentially of acetanilid, caffeine, aloin, atropine sulfate, and capsicum. The presence of acetanilid in the amount found was sufficient, said the Commission, to render the product dangerous if used as prescribed. Frequent or continued use of acetanilid might cause serious blood disturbances, anemia, or collapse. The shipper failed to claim his product, so it was ordered destroyed.

"Doctor's Daughter" tablets were white and pink; the white tablets consisted of calcium carbonate, sodium carbonate, and sodium bicarbonate; the pink tablets consisted of belladonna, alkaloids, including atropine, and laxative plant drugs. The product was held to be misbranded since it failed to carry adequate warning statements concerning the effects of continued use of these tablets or their effects under certain conditions. Since no one claimed the tablets they were ordered destroyed.

[1] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act*, February, 1943, Case 31,157. and November 1942, Cases 560, 562, 564, 569, 296, 550.

A product labeled as a "Natural Diuretic Eliminant Water" was found upon analysis to be a "slightly mineralized water similar in composition to Ohio River water."

Represented as a substitute for the secretions of the pancreas which would be helpful in the relief of suffering diabetics and as containing a potency equal to two insulin units, Crawford's Ridia was found upon analysis to consist essentially of alfalfa with smaller proportions of mint.

A nationally advertised cereal was held to be misbranded because it created the impression that it contained Vitamins A, B_1, C, D, and G in consequential amounts, when in fact their presence was inconsequential; that it would be effective in preventing colds and infection, in producing healthy nerves, normal growth, good teeth, strong bones, and other desirable attributes, when in fact it would not be effective in producing any of these results. Again the product was unclaimed so it was delivered to a nearby Federal institution, the inmates of which were no doubt permitted to eat it without illusion.[1]

These random illustrations are typical of the type of fraudulent action against which the Food and Drug Administration is constantly on the alert. There is no way of knowing how many such products escape detection, but we do know that the number discovered runs into the thousands.

The danger of self-medication by using concoctions whose content is unknown is serious. A mysterious new blood disease known as agranulocytosis which destroys the white blood cells and usually ends fatally has been traced to the use of amidopyrene in patent medicines for the relief of headaches and pains in general. This disease killed 1,300 people in three years.[2]

Four years after the introduction of dinitrophenol, a comparatively new anti-fat drug, it was estimated that 100,000 American women were using it as a reducing remedy. It was advertised to stimulate metabolism, literally burning up excess fat. What was not advertised is that twelve San Francisco women had been stricken with temporary blindness believed to have been caused by use of this drug. Some physicians contend that women using it may expect their children to be born with eye cataracts, atrophied livers, or other defects. In New York this drug is sold only on prescription, but in many states it is sold without restriction.[3]

According to one medical practitioner and writer, "There is no such thing as a safe and reliable drug remedy for obesity." Most of the preparations used in baths for weight reduction consist of baking soda or perfumed Epsom salts, a combination which sells for 20 to 50 times the

[1] *Notices of Judgment*, *op. cit.*, November, 1942, Cases 541, 553, 554, 575, 577, 580.

[2] *New York Times*, June 8, 1935.

[3] *New York Times*, July 10, 1935, June 7, 1936

original cost. Any effect they may have depends solely upon the hot bath which induces perspiration. The Texas Guinan Obesity Cure was finally stopped by a postal fraud order. Texas Guinan had sold her name to a promoter for $500 down and $50 a week. The "cure" consisted of 30 cents' worth of powdered alum in alcohol and water, and sold for $20.[1]

According to Dr. Solomon any advertised remedy for diabetes, other than insulin, to be taken through the mouth is a fraud. "Practically speaking, all remedies for such weaknesses are fakes." Banbar, prepared by a man who had formerly been a shirt salesman, was advertised as a remedy for diabetes. It consisted of an extract of horsetail weed, small amounts of Epsom salts, potassium acetate, Bar-berry, May-apple, strychnine, and lettandra. This concoction sold for $12 a bottle. In 1928 it was estimated that mail order medical cures of this type mulcted the public out of $100,000,000 annually.[2]

The structure of the patent medicine business rests to a very large extent on advertising. In fact, the manufacturers of "many patent medicines spend half or more of their gross incomes on advertising."[3] A man whose life has been spent in the advertising business explains that patent medicine advertising falls into two periods, one before the Civil War and the other after. Although the industry was large before 1860 "it became tremendous after the Civil War." The wounds, fevers, ailments, and general complaints of returning soldiers made them receptive customers for patent medicines and self-medicating advertising. Although huge fortunes were acquired by patent medicine producers, those newly rich people were not received in the highest social circles. "To the more intelligent members of the community there was apparent a fraud and an exploitation of ignorance that made the nostrum manufacturer a person whom those engaged in more proper activities did not care to meet socially."[4]

Dentifrice Frauds. In one recent year there were more than 700 brands of tooth pastes or tooth powders on the market and consumers spent somewhere between $50,000,000 and $70,000,000 on dentifrices. In spite of the large variety of brands available, only eighteen were found in most stores, including those advertised at great expense.

Making consumers conscious of their teeth is a splendid illustration of nealth. The teeth are vital living organs whose soundness depends on diet and general good health. Contrary to dental advertising, clean teeth do decay. Only one person out of four has pyorrhea, rather than four

[1] SOLOMON, Charles, *The Traffic in Health*, pp. 184, 185, 198, Navarre Publishing Co., New York, 1937.
[2] *Ibid.*, pp. 266, 268–269, 277; 52.
[3] *Ibid.*, p. 25.
[4] PRESBEY, Frank, *History and Development of Advertising*, pp. 291, 296, Doubleday Doran & Co., Garden City, New York, 1929.

out of five; and that disease is not caused by any one bacterial organism, nor can it be prevented or cured by nostrums. Tooth pastes or powders alone cannot cleanse anyone's teeth. Brushing serves to clean teeth, and to stimulate circulation of blood. A dentifrice is merely a toilet accessory rather than a therapeutic agent. Consumers could get equally good results at much lower cost by using a simple mixture of salt and baking soda or by having their local druggist compound a paste or powder. On page 45 of *Paying Through the Teeth*, Dr. Palmer gives a formula which, prepared by one's local druggist, would cost about 80 cents a pound as compared with $2.00 a pound or more for advertised powders in fancy tins. If for some reason one insists on having a commercial preparation, then the least he should do is to write to the Council on Dental Therapeutics, American Dental Association, 222 East Superior Street, Chicago, Illinois, for a list of its approved dentifrices, which numbered only twenty-six powders and pastes in a recent typical year. One will not find many nationally advertised brands on the Council's list. In the April, 1943, list there was just one. Nor will one find the fourteen brands commonly sold in drugstores.

Under its expanded powers the Federal Trade Commission has proceeded against dentifrice manufacturers who claim too much for their product. One firm agreed to stop advertising that the use of its dentifrices would contribute to the prevention of tooth decay. Another firm agreed to stop advertising that its "powder would assure the possession of teeth that are white, clear, and sparkling or will assure beautiful teeth or teeth that are as beautiful as those of some movie stars. . . . " They agreed further to stop advertising that their product would clean the surfaces between the teeth, that it would liberate nascent oxygen in the mouth, that it would prevent film on teeth or decay of the teeth, that it would remove all types of stain, that the use of powder is more effective in cleansing the teeth than toothpaste, that movie stars use their product to the exclusion of all other dentifrices. Still another manufacturer was ordered to stop advertising that its dentifrice is a competent or effective germicidal or antiseptic agent, that it will kill all harmful bacteria in the oral cavities, that it will remove stains from the teeth, that it will keep the teeth and mouth clean, or that it will brighten or restore the brightness to teeth.[1]

Mouthwashes are among the most useless of modern frauds. If they are strong enough to destroy germs they will destroy delicate tissues also. Since food and drink inject fresh bacteria into the mouth the antiseptic properties of any mouthwash are effective for only a short time. More-

[1] Federal Trade Commission, *Decisions*, vol. 34, Case 02049; vol. 30, Docket 3791; vol. 29, Docket 3587.

over, most mouthwashes are so weak as to be useless. One widely advertised product is composed chiefly of alcohol and water with a little boric and benzoic acid. A penny's worth of carbolic acid possesses the antiseptic properties of $15 worth of this mouthwash, while a penny's worth of corrosive sublimate has the antiseptic action of $495 worth. The actual ingredients of another brand cost less than one cent, yet this preparation, which is about as effective as a solution of common salt, sold for 85 cents a pint.

Comparative reading of advertisements for tooth powders and pastes should serve effectively to show how extravagant claims cancel out. Essential ingredients of any dentifrice are calcium carbonate, soap, saccharine, and a distinctive flavoring such as oil of peppermint. One commercial formula varies this by adding potassium chlorate, a 2½ ounce tube containing 30 grams of this poison. Since 8 grams taken in one dose may prove fatal this is enough to kill at least three people. While it is not likely that any normal adult will swallow the contents of an entire tube, this is an extremely dangerous preparation to have within reach of children. The very best that can be said for it is that it is fraudulent, since potassium chlorate is unnecessary in caring for healthy teeth.

Teething lotions are a particularly vicious form of fraud. Crying children are quieted by various brands containing from one third to one seventh of a grain of morphine. Others contain as much as three grains of opium or 12 per cent of alcohol.

The color of teeth depends on diet and general health. Discolored teeth may be quite healthy, while dazzling whiteness is not necessarily an indication of good teeth. Popular belief encouraged by dental advertising supports the belief that health and beauty are reflected in white teeth. This has resulted in a large sale of bleaches. Bleaching can change the color of one's teeth, but only by using such strong chemicals that the teeth are injured. Containing from 5 to 16 per cent of citric or hydrochloric acid, these bleaches may destroy tooth enamel and lead to decay. Yet diluted with colored water they are sold at exorbitant prices.[1]

Buying Beauty. "Cosmetic," from the Greek, means skill in decorating. As a noun it means any external application intended to beautify the complexion or hair. Use of cosmetics is as old as feminine search for artificial beauty. The basic appeal underlying their use is probably the desire to appear attractive to the other sex. As in the case of health and teeth, real beauty results from proper diet, proper elimination, and external cleanliness. Enlarged pores, blackheads, pimples, or sallow

[1] This discussion has been based largely on PALMER, *Paying Through the Teeth*, a book well worth reading.

complexion are the superficial indications of an unhealthy system. Cheap nostrums applied to the surface may cover up such blemishes but are quite ineffective in eliminating the cause. Good, wholesome food in proper variety and amounts will contribute to recovery from the ill health and the constipation which underlie so many skin afflictions. Good soap and water will do more than a dozen preparations in cleansing the skin, while cold water is probably the best known astringent.

Nevertheless, a $400,000,000 annual business is based on representations that beauty can be bought in jars, bottles, or packages. In return for their money women buyers get about 50,000 tons of cleansing cream, 27,000 tons of skin lotion, and 20,000 tons of complexion soap. These large amounts of cosmetics are compounded according to formulae which are fairly standard and available to every manufacturer. It might be supposed that every firm making cosmetics would have in its employ at least one manufacturing chemist, but such is not the case. In fact, quite a number of so-called manufacturers do no manufacturing but have their products made up for them by a manufacturing chemist.[1] This means, of course, that the only difference among some cosmetics is to be found in the container, but of course the consumer buyer does not know that, unless she has inside information or depends on a consumer testing agency for guidance. The poor maiden suffering social ostracism because of her pimples, chafed hands, or body odor is told that she can surround herself with male admirers by purchasing and using an ordinary soap priced at 25 or 50 cents for a small cake. There is probably no field in which advertising claims are more extravagant, misleading, and fraudulent. The industry is infested with charlatans who prey on gullible consumers under the guise of science. To these pseudo scientists who do not know one ingredient from another research means spending a day in the public library among recipe books, while chemistry means ability to analyze and duplicate a competitor's product.[2]

All this is not to imply that good cosmetics do not have their place, but rather that their function is very limited. Not only are the claims made for most cosmetics grossly misleading, but the ingredients in many are positively harmful. Moreover, practically all preparations are greatly overpriced. Advertising and fashion have been used to bolster up an artificial demand at ridiculous prices. Ordinary cold cream, face powder, talcum, and rouge may have their legitimate uses, but a good cold cream can be prepared by a druggist for about 60 cents a pound. Some widely advertised brands sell for $5 or $10 for a jar containing a few ounces.

[1] MILLER, Lois Mattox, "Cosmetic Comedy," in *The American Mercury*, March, 1939; condensed in *The Reader's Digest*, March, 1939, pp. 18–20.

[2] *New York Times*, July 23, 1935.

At best a cold cream is a supplementary cleansing agent; none of them can feed skin or tissue as claimed.

Assertions to the contrary were permissible before 1938, but the Federal Trade Commission has insisted that such claims in advertising must now be discontinued. For example, a large New York cosmetic firm was ordered to stop advertising that any of its cosmetics, facial creams, or toilet preparations will serve as food for or nourish the skin, muscles, or tissues; that they will prevent wrinkles, or strengthen the eye nerves; that they contain living sparks of life which increase their therapeutic value; that they will rebuild worn-out cells; or that they will dissolve fatty tissues or act as weight reducers. Another firm, a national advertiser, agreed to stop advertising that its cream would restore oils to the skin, reclaim the skin, overcome oiliness of the skin, cause blackheads to disappear, nourish the skin, or keep it healthy. In all, the firm agreed to stop representing 30 such claims for its products. Another well-known firm agreed, under pressure from the Federal Trade Commission, to stop advertising that its cosmetics would affect the contour of the face, would prevent or eliminate wrinkles, would preserve a youthful throatline, or that they would banish fatigue, and so on through twelve stipulations. Still another cosmetic corporation agreed to stop advertising that certain of its products would remove brown spots, freckles, or other discolorations; that they would give a clear, young, or fresh skin; or that they would stimulate circulation. The final case to be mentioned is that of a corporation which advertises nationally. It has been ordered to stop advertising that its facial powder will guard against or prevent skin blemishes or infection from germs; that its powder will spread farther than other competitors' powders of comparable quality; that its cold cream will remain sterile or that it will kill germs or prevent germ growth; that its creams or soap have any added beneficial value upon the skin by reason of their vitamin content.[1]

All of the foregoing is well summarized in the following statement by a medical authority: "No drug, chemical, glandular, or other medicinal agent added to a facial cream can enhance its value, improve its quality, or transform it into a tissue-builder, a rejuvenator, or a revitalizer." The same writer says elsewhere that excellent Kaolin can be purchased from a druggist for 10 cents a pound. A manufacturer of cosmetics will add a little glycerine and water and a dash of perfume to the Kaolin and sell it to the consumer in a jar at a price ranging from \$2 to \$10.[2]

Astringents are advertised to refine enlarged pores, yet none can

[1] Federal Trade Commission, *Decisions*, vol. 27, Docket 2939; Case 02191; vol. 28, Case 02357; vol. 33, Docket 4254; Case 02873; Docket 3438.

[2] SOLOMON, *op. cit.*, pp. 294, 306.

do so any better than plain cold water. Chief ingredients are alcohol and water. A certain skin tonic consisting of grain alcohol, a basic acid, a dash of perfume, and plenty of water costs not more than 3 cents and sells for 85 cents. Another preparation costing $\frac{1}{2}$ cent to make is advertised and sold for one dollar.[1] Four brands of astringents had about 23 per cent alcohol and were substantially the same except for color and odor. Yet their prices ranged from 6 to 26 cents per ounce.[2]

Fashion dictates varied colored nail polishes for every occasion and costume; and at least eight shades are available. A tiny package containing 11 cubic centimeters, costing $\frac{2}{10}$ of a cent for ingredients, sells for 29 cents. Other brands costing about the same amount vary in price from 25 down to 10 cents.

Hair, like skin, is a part of the body organism whose health and appearance depend on general bodily health. For most people all that is needed is regular washing with good soap and water. Men, being particularly susceptible to baldness, are the special victims of quack preparations guaranteed to save or restore hair. Ability of any of these products to accomplish such results may be judged by a widely advertised hair tonic, consisting of 14 per cent alcohol, 36 per cent coal oil, and a bit of quinine sulphate, with a dash of perfume. This product, priced at $1.50 for a four-ounce bottle, actually cost only 20 cents a gallon to produce, or less than 1 cent for four ounces.[3]

While women crave beautiful hair on their heads they despise its growth on other exposed parts of the body. Men go to considerable pains to shave hair from the face, but consider a heavy growth on chest, arms, and legs as an indication of strength and manhood. These paradoxical practices can be explained, if at all, only by custom or fashion. In Puerto Rico, for example, it is reported that "girls take pride in hair on their legs."[4] Perhaps some day fashion will encourage superfluous hair for all women. If it does, a sizable industry will be destroyed. There is no preparation which can remove hair permanently and safely. The various concoctions which it is claimed will do so are all frauds, according to Dr. Solomon. Exposure to the sun and wind, as well as shaving and the use of depilatories, stimulates the growth of excess hair.[5] The electrolytic needle can remove hair permanently but the operation is costly, painful, and dangerous. Any chemical preparation strong enough to kill hair will injure the skin. If women insist on removing what they call superfluous hair the only safe and economical method is to shave it off. Popular belief holds that shaving makes the hair bristly. This belief is based on

[1] PHILLIPS, *Skin Deep*, chaps. 1, 6.
[2] MILLER, *op. cit.*, p. 20.
[3] HARDING, *The Popular Practice of Fraud*, p. 55.
[4] *New York Times*, May 16, 1940, p. 28.
[5] SOLOMON, *op. cit.*, p. 312.

the fact that a man's beard feels stiff. Permitted to grow, however, it will be as soft as any other hair. It is not the shaving, but rather repetition of the practice, which gives the illusion of stiffness.

One of the most widely advertised preparations for removing superfluous hair was a product devised by a former operative in a beauty parlor, which sold for $10 a jar, although the cost was only 35 cents. In one year 120,000 jars of this preparation were sold through department stores alone. Its main ingredient was thallium acetate, a deadly poison, long used for extermination of rats and squirrels. In fact there is no known antidote for it. While sales of that product were at their height doctors the country over reported cases of serious illness which was traced to its use. By July, 1932, the manufacturer went bankrupt with liabilities of nearly $2,500,000, the greater part of which represented damage claims by injured users.[1]

Equally dangerous is the dictate of fashion that women should subject eyebrows and eyelashes to artificial treatment. Use of one preparation for this purpose, advertised as safe and harmless, resulted in seventeen cases of injury reported by the American Medical Association. One of these was a case of total blindness and one resulted in death.[2] Until 1938 there was nothing to prevent any persons from manufacturing and marketing such dangerous products even though they had had no education as to drugs. The only redress a victim had was a damage suit in a court of law. Obviously money damages can never repay for suffering, blindness, or death.

American standards of beauty demand a slender figure. Fat people are funny. Here again the standard may change, but until it does thousands of people, particularly women, will continue to jeopardize their health and even their lives by using dangerous quack preparations guaranteed to make them slim. These preparations vary from simple pseudo-scientific diets to the use of dangerous cathartics and drugs. One of them substitutes tablets for food, the tablets consisting of soya bean flour, flavored with cocoa and salt. Costing about $2\frac{1}{4}$ cents a can they retail at $1 and $2. A certain "herb tea," an example of the purgative type of reducer, consists almost entirely of pure senna leaves, a powerful purgative. A package costing 15 cents to make sells for $1.50. The basic ingredient of another preparation is desiccated thyroid, together with three cathartics. The history of efforts to control the activities of the promoter of this product is too long to recite here, but is well worth reading in detail as an illustration of utter lack of consumer protection.[3]

It will be recalled that Betene, mentioned on page 207, and adver-

[1] PHILLIPS, *op. cit.*, chap. 9. LAMB, *American Chamber of Horrors*, p. 29.

[2] LAMB, *op. cit.*, chap. 2, pp. 18–23.

[3] PHILLIPS, *op. cit.*, chap. 13.

tised as an aid in weight control, consisted of a mixture of dried skim milk, dried egg yolk, soybean tissues, wheat bran and wheat germ, salt, agar agar, calcium phosphate, chondrus (Irish moss), and saccharin flavored with cocoa, vanillin, and coumarin, together with certain added vitamins. Products of this type persist even under the new Federal Food, Drug, and Cosmetic Act. Two brands of candy were seized by the Food and Drug Administration on the charge that they misrepresented falsely their efficacy as a reducing agent. In the case of one, it was alleged that it would be possible for the consumer not only to reduce weight pleasantly and without effort but to keep weight down to the desired figure and to cut down on the amount of food intake without feeling pangs of hunger, distress, faintness, or debilitation. Although the shipper was known in these cases, the firm did not appear to claim the product, so it was ordered destroyed.[1]

Service Frauds. In a book which shocked the complacency of some of America's 32 million peacetime motorists, Roger Riis and John Patric reported their findings based on a nation-wide survey of practices prevailing in automobile service stations. They reported that their investigation permits but one conclusion—automobile service stations do not give their customers a square deal. Riis and Patric also tested the honesty of 304 radio repair shops. Presented with a radio in which the only thing wrong was a loosened tube, 195 of the 304 shops tried to take advantage of the customer. Surveys of watch and typewriter repairmen yielded similar results.[2]

Miscellaneous Frauds. Consumer buyers of silk want that product for its beauty and comfort, but those who sell it are seeking profit. When the gum is removed from raw silk from 16 to 20 per cent in weight is lost. The practice of restoring this loss in weight has grown to the point where as much as 75 per cent of so-called silk consists of added weight. This is accomplished by passing the product through a bath of mineral salts. Tin is used most commonly, but lead is being used increasingly, thereby adding an element of danger from poisoning. Weighted silk cracks and splits and feels clammy and hot rather than cool and comfortable in warm weather. Since genuine silk is heavy, consumers are easily deceived by the practice of mineral weighting.

Misrepresentation of furs is prevalent, and until the Wool Products Labeling Act was passed in 1939 a large portion of so-called woolen products consisted of substitutes. Some liquid shoe polishes and dyes

[1] Federal Security Agency, Food and Drug Administration, *Notices of Judgment under the Federal Food, Drug, and Cosmetic Act,* November, 1942, Cases 592, 593, 594, 595.

[2] Riis, Roger W., and Patric, John, *The Repairman Will Get You If You Don't Watch Out,* Doubleday, Doran & Co., Garden City, New York, 1942.

contain nitrobenzine, a poisonous ingredient which may cause illness or even death if applied while shoes are being worn. "Solid mahogany" furniture is mostly veneer. An effective insecticide should contain a pound of pyrethrum powder, costing 50 cents, to a gallon of kerosene, costing 14 cents, but the formula of one widely advertised preparation calls for one pound to 120 gallons. The retail selling price of such insecticides is about $4 a gallon.

Making a routine tour of retail clothing, food, and fuel stores in the boroughs of Manhattan and Queens in New York City, the Commissioner of Markets was overcharged or short-weighted in seven out of nine transactions. He purchased women's stockings labeled "silk" which turned out to be a cheap substitute; he was charged 18 cents a pound for chickens although the window sign read 16 cents; having ordered and paid for five gallons of gasoline he was given four gallons, seven and one half pints. The Director of the City Bureau of Weights and Measures reported that seven summonses a day for violations of this kind is not an unusual number. It was his thought that any consumer buyer might have a similar experience on the same number of transactions any day.[1]

One of the most common ways of defrauding consumer-buyers is to deliver smaller quantities than have been paid for. The problem of short weights and short measures is discussed in Chapter 26.

Why Does Fraud Persist?

Gullible Consumers and Greedy Producers. Fraud is as old as the human race and changes, if at all, only in forms and amounts. Frauds of a generation or a century ago have given way to newer and possibly better frauds; better at least for deceiving modern consumers. They are probably no more clever, for very few frauds are or need to be clever. The country is full of people who believe anything. Such childish belief is based on ignorance or naïveté. Among predatory producers such people are easy prey. Craving health, wealth, beauty, or power, people like to believe that a simple mixture of water and alcohol will cure an incurable disease, or that an advertised remedy will make them thin. They do not stop to analyze such propositions. If they did the fraud would be apparent. Rather they act on emotion, a dangerous guide in the market place. Such persons are as selfishly seeking something for nothing as is the one who sells the worthless preparation or product.

All consumers are ignorant in varying degrees. Some are aware of their predicament, but many are not. The latter type of buyer is much more easy to deceive. Evidence presented not only in this, but in other chapters, is certainly sufficient to demonstrate the utter inability of con-

[1] *New York Times*, November 4, 1939.

sumers in general to be wary in the market place. Only chemists can analyze some products, and sometimes they have difficulty. Even though merchandise may be represented honestly, scarcely a buyer has any way of judging the validity of its price. Many dealers keep this in mind as they set the retail prices for their merchandise and services.

In an economic organization definitely dedicated to consumer welfare individual ignorance of the market place would not be serious. Consumers could pool their knowledge and buy with assurance that merchandise offered for sale was honest, reliable, and fairly priced. But the system in which consumers now live is dedicated primarily to making profit for producers. Extravagant profits are easily and quickly made with a small capital investment by selling something for $5 or $10 which costs 30 cents to make.

Not all producers are greedy, but certainly many of them are. Not all greedy producers are utterly devoid of conscience, but many of them seem to lack any sense of social responsibility. Persons who make poisonous products which kill and maim their users may be operating within the limits of law, but not within the restrictions of any code of ethics. Growth of a large impersonal market has rendered it easier for conscienceless producers to ply their trade, not only because detection is more difficult but because personal relationships with gullible victims are unnecessary. Whenever an injured person does sue for damage he is treated as a case rather than as a consumer.

Impotent Laws. Caught between the two horns of this dilemma, consumers need protection from their own ignorance and from the avarice of predatory producers. It is futile to talk of educating consumers. No one person can ever be sufficiently trained in all fields of knowledge to combat the specialized skill of profit-seeking producers. The best that can be done is to develop a body of wary consumers. This needs to be supplemented by their collective power through the state in the form of law. Yet consumer ignorance makes it difficult to enact and to enforce legislation. The problem of consumer protection is further complicated when laws are defective and authority is divided among local, state, and Federal governments. Effective legislation is difficult to secure not only because uninformed, unorganized consumers fail to demand it, but because small well-organized and well-informed groups of businessmen oppose it. In the view of these men the right of free enterprise carries with it the unrestricted right of exploitation. Punitive provisions of such laws as are on the statute books are absurdly lenient. Rarely is the vendor of a fraud committed to jail, while fines are so small as to become nothing more than an additional cost of doing business.

Advertising Fraud. It has been estimated that false and misleading

advertising costs consumers $500,000,000 a year. This is probably a very conservative estimate. With growth of a large-scale market the individual vendor of quacks and nostrums characteristic of former days would be much less effective without modern advertising. It is interesting to observe that American insistence on compulsory education has inadvertently played into the hands of fraudulent advertisers. This has come about in two ways. By enabling practically all people to read it has become possible for advertisers to carry their message to many more people. A second result of national literacy has been the development of magazines and newspapers with national circulation which go into the homes of millions of potential buyers. The most recent development and one which is growing by leaps and bounds is the use of radio. This device not only leaps over the obstacles of literacy and the failure of many people to read, but adds the semipersonal appeal of the salesman's voice.

Summary

From a consumer point of view any artifice by which one's right or interest is injured is fraud, but at law the definition of fraud is restricted to those cases where deliberate intent to deceive can be proved. This, together with ineffective competition and the growth of a large, impersonal market, has led certain profit-seeking producers to resort to the manufacture and sale of numerous fraudulent products as a means of securing easy income. There is scarcely a field of human want which has not been exploited. Specially attractive fields have been the preparation and sale of food, health restoratives, dental devices, beauty aids, and repair services. In all these cases custom, fashion, and advertising have supported absurd claims.

Gullible, selfish consumers seeking something for nothing share responsibility for the prevalence of fraud with greedy producers eager for profits. Protective laws are difficult to enact and to enforce without wide public demand and support. In recent years advertising has become a pillar in the house of fraud. Public regulation of this powerful force has become imperative.

QUESTIONS FOR DISCUSSION

1. Do you practice the slogan of the market place, "Let the buyer beware"?
2. Have you ever been defrauded, economically? Legally?
3. How capable do you think you are of detecting fraud?
4. Have you ever purchased a patent medicine? Why? With what results?

5. When you purchase a packaged article do you ever read the label? Are labels reliable?
6. Do you know anyone who has used a reducing preparation? With what results? Did that consumer know the contents of the preparation?
7. Is the dentifrice you use approved by the American Dental Association?
8. What do you spend annually on cosmetics? Do you get your money's worth?
9. Can you give additional illustrations of fraud, based on your experience or observation?
10. Do you think that honesty is the best policy in business? Does it always pay?
11. Do you have any responsibility for the prevalence of fraud?
12. How does the practice of fraud compare with the economic theory of market organization and practice?

PROBLEMS AND PROJECTS

1. Interview the secretary of your Chamber of Commerce or Better Business Bureau; secure information for a report on recent local frauds investigated.

2. Ask the editor or advertising manager of one of your local newspapers to tell you what standards of honesty and reliability are applied to proffered advertisements; check these statements with current advertisements running in the paper.

3. Choose five advertisements, in nationally circulated magazines, which you regard as fraudulent; give reasons for your convictions. Could you prove fraud in a court of law?

4. Digest several Federal Trade Commission decisions dealing with fraud.

5. Digest the last issue of *Notices of Judgment*, classifying cases according to various types of fraud.

6. Look up the Marmola case in Federal Trade Commission decisions or the B & M External Remedy case in *Notices of Judgment;* in your report emphasize the difficulty of proving legally the fact of fraud.

7. Review one of the thirteen books on fraud, listed on page 203.

8. Study the unit "Fur," or some other unit, in Reich and Siegler's *Consumer Goods*, and find to what extent consumers can learn how to test goods and to detect fraud.

13

Price Appeal

What Is Price?

A Monetary Measure of Exchange Value. The centric problem in any economic question is that of value. In an economic system in which goods are scarce in relation to human wants the problem of valuation emerges. This problem is to discover the factors which determine the ratio at which scarce goods exchange in the market place. Through the price system values are expressed in monetary terms and scarce goods are apportioned among consumers.

Traditional treatment of value assigns to consumers the important role of guiding the economic system. Presumably acting as economic men, they express their choices in the market place. If they want more of certain commodities, the prices of those commodities will rise and more will be produced; if less of certain commodities is wanted, their prices will fall and producers will curtail their output. Conversely, at the very time prices are rising as an indication of increased consumer demand their effect is to discourage buying; on the other hand, as prices fall, warning producers to curtail output, consumers are encouraged to buy more. The chief defect in this theory, aside from the unsound assumptions on which it is based, is not that it fails to recognize the importance of consumers, but rather that it fails to analyze the forces influencing consumer choice.

Objective exchange value is the power of a commodity to command other goods in exchange. If a loaf of bread exchanges for one coca-cola the value of bread is one coca-cola, while the value of one coca-cola is one loaf of bread. To avoid obvious limitations of a barter system of exchange some special commodity is used as money to serve as a medium of exchange. Then the values of the bread and of the coca-cola are measured in terms of this medium; each may be valued at and exchanged for ten cents.

Temporarily this value is determined by the willingness of consumers to buy. If the supply of bread were definitely limited its price would be determined by the importance of the last loaf to that buyer whose purchase would clear the market. In case of an emergency resulting in a definitely limited supply of bread and coca-cola one could safely

predict that in a freely competitive market the price of bread per loaf would soar, while the price of coca-cola would fall.

Over a period of time supplies of goods are variable. Consequently, consumers do not have full power in determining prices. While producers will take temporary losses, in the long run prices which they receive must cover their costs of production. Otherwise those producers on the borderline who cannot meet their expenses are forced out of business. Supplies are thereby diminished and in the face of a constant demand prices rise.

Is Price an Accurate Measure of Value? By definition price is a monetary measure of value. If the price of bread is quoted at 10 cents a loaf that price is a measure of the exchange value of bread regardless of any other measure which may be applied. The validity of price as an accurate measure of value is limited by the validity of certain basic assumptions.

One of these basic assumptions is that competition prevails among producers and consumers. Competition may be defined as rivalry in buying and selling. Obviously wherever such rivalry is missing the above explanation of value determination simply does not fit. By the very nature of their motivation producers are prone to combine to avoid rivalry and thus gain greater profits. A producers' paradise would consist of a perfect monopoly over a product universally needed by consumers regardless of price.

A second basic assumption is that consumers are economic men able to judge price and quality. Considerable evidence has already been presented which goes to show that very few if any consumers function as economic men.

A third assumption is that subjective valuations are translated into objective values in the market place. Subjective value is the importance which an individual consumer places on a commodity. This may or may not bear a close relation to its market value. If all consumers were equally skillful in bargaining and possessed equal purchasing power this assumption would be valid. Actually there is wide variation both in the bargaining ability of consumers and in their purchasing power, depending on their varying incomes.

The law of demand holds that the quantity of an economic good that will be purchased varies inversely with price. This means that if price is high consumers will buy smaller quantities, while if price is low they will buy larger quantities. In many cases, however, consumers are positively attracted by high rather than low prices. This may be explained by their desire to purchase in order to display their pecuniary power. Among lower-income groups it may be explained by emulation. Or

being unable to determine quality, consumers may rely on high price as a measure of quality.

One Price or Many Prices?

Is the United States a One-Price Country? There is an interesting and significant difference between the price systems of Orientals and Occidentals. In large areas Orientals still use the bargaining system extensively. Under this plan no price is set on a commodity. When a prospective buyer approaches a prospective seller the latter is asked what price he expects to receive for whatever he has to sell. In quoting his price the prospective seller asks for what he would like to receive. The prospective buyer then parries with an offer of the lowest price for which he hopes to secure the article in question. Neither seller nor buyer expects to strike a bargin on the basis of these preliminary offerings. In the Near East the usual practice of buyers is to offer approximately one third of the asking price. Agreement may be reached finally on a figure about one half of the original quotation. Thus if the price which a seller asked were $1 the buyer would counter with an offer of 30 or 35 cents. Depending on a number of variable factors, the final exchange price would be approximately 50 cents.

Under such a plan real competition prevails. Not only sellers but buyers are on the alert. Even so, all buyers are by no means equal in their bargaining ability. Such ability depends upon a variety of factors, including early training and experience, physical appearance, and ability to judge when the seller has reached his bottom price. A too prosperous personal appearance is fatal to effective bargaining, while real ability to judge exchange value is essential. Nothing is more pathetic than to watch a Westerner deal with an Oriental. The former, quite unaware of the real value of merchandise, relies on price as a measure of quality. This plays into the seller's hands beautifully, the buyer being accommodated by the quotation of an unusually high price. When tourist ships drop anchor in an Oriental harbor permanent residents of the city make no effort to go shopping. While sellers enjoy a field day with the visiting tourists from the West, other buyers declare a temporary moratorium.

Those accustomed to the one-price system complain that the bargaining system is a terrific waster of time. This is particularly objectionable to Americans, whose high regard for time reflects their producer background and viewpoint. To the Oriental time is less important, while buying is a game as well as an economic duty. Americans whose economic philosophy is that of promoting their welfare as consumers by increasing their output as producers are accustomed to spending all

their time and energy in attempting to produce more. This leaves little time and no inclination to enjoy the art of bargaining.

Consequently consumers in the United States follow the one-price system. Under this plan retailers add their markup to their wholesale cost to determine the price at which they are willing to sell. That price is then marked on the merchandise or on a tag where any prospective buyer may see it. Having full and free opportunity to examine the merchandise to the best of his ability, he may then make up his mind without interference by the seller as to whether he is willing to pay the price asked. Presumably, if the price is too high the prospective buyer will purchase elsewhere. Concerted action of this kind by a large number of consumers is supposed to force the offending retailer to lower his price.

"Law" of One Price. Long ago this led economists to formulate the "law" of one price, according to which in a given market at a given time there can be but one price for a given commodity. Assuming competition, this means that price serves as a guide to quality. This method also results in a considerable saving of time, although it should be remarked that the bargaining system in the Orient does not apply to small items or to those which are purchased regularly.

The Lure of High Prices. Unfortunately for American consumers, the blunt truth is that they do not usually compare prices in different stores before buying. Retailers have learned that prospective buyers do not shop around. Typical of such buyers is the housewife who purchases her food supplies over the telephone. Instead of shopping, such a buyer merely places an order. In such cases the only limit to a retailer's markup is his judgment of what the traffic will bear. Such statistical evidence as is available shows that the traffic will bear a pretty heavy load. Retailers also have learned that very few buyers can judge quality. As a matter of fact there is much evidence to show that retailers themselves cannot do so. This weakness of consumers is capitalized by retailers. High price is advertised as a quality guide. Americans are quite completely committed to the idea that you get just about what you pay for, even though subsequent evidence will show the fallacy of this belief. Retailers have learned to their advantage that some buyers are positively attracted by high prices. Most of us know persons who are proud of the high prices they pay. Such people are afflicted with a desire to display their power to pay, an affliction which retailers nourish and to which they cater. If buyers expect to pay high prices one could hardly expect a retailer in business for profit to disappoint them. That they do not is illustrated by the statement of a Middletown retailer in women's clothing. Assuming identical style, the question of whether women would buy a higher- or lower-priced garment was answered in the following way:

TABLE IV.—COMPARATIVE PRICES ASKED FOR EIGHTEEN IDENTICAL GROCERY PRODUCTS BY RETAILERS IN THREE OHIO MARKETS IN APRIL, 1933*

Product	*Granville*				*Bexley*				*Columbus*			
	Independent	Chain No. 1	Chain No. 2	Maximum Variation	Independent	Chain No. 1	Chain No. 2	Maximum Variation	Independent	Chain No. 1	Chain No. 2	Maximum Variation
	cents	*cents*	*cents*	*per cent*	*cents*	*cents*	*cents*	*per cent*	*cents*	*cents*	*cents*	*per cent*
Baking Powder (Royal)	45	41	45	9.7	39	41	45	15.4	45	41	45	9.7
Chocolate (Baker's)	28	23	23	21.7	23	23	23	0	24	23	23	4.3
Cocoa (Hershey's)	15	10	10	50	13	10	10	30	10	10	10	0
Coffee (Maxwell House)	35	30	30	16.6	32	30	30	6.6	30	30	30	0
Ginger Ale (Canada Dry)		25	3 for 49	53	20	20	25	25	20	20 or 3 for 49	3 for 49	22.4
Tea (Lipton's) ($\frac{1}{4}$ lb.)	20	19	21	10.5	22½	19	21	18	18	19	21	16.6
All Bran (Kellogg's)	25	19	19	31.5	19	19	19	0	20	19	19	5.2
Puffed Wheat	13	9	9	44.4	10	9	9	11.1	12	9	9	33.3
Crisco	25	19	20	31.5	20	19	20	5.2	20	19	20	5.2
Maraschino Cherries (8 oz.)	18	19	21	16.6	20	19	21	10.5				
Flour (Gold Medal) (12½ lb.)	35	45	43	28.6	44	39	43	12.8	46	45	43	7
Buckwheat Flour (Aunt Jemima)	18	2 for 25	10	80	15	2 for 25		20	10		13	30
Bisquick	35	29	32	20.7	32	29	32	10.3		29	32	10.3
Gelatin (Jello)	3 for 25	3 for 25	7	19	3 for 25	3 for 20	2 for 15	25	3 for 25	3 for 25	7½	11.1
Soap (Ivory guest)	6	3 for 13	3 for 10	80	6 for 25	4 for 19		14	12 for 50	5 for 19	5 for 19	9.6
Fels Naptha	7	5	10 for 54	40	10 for 49	5	5½	12.2	5	5	5½	10
Soup (Campbell's)	10	2 for 19	8	25	10	2 for 19	8⅓	20	9	2 for 19	3 for 25	14
Sugar (Confectioners')	10	3 for 25	7	42.8	9	2 for 15	7½	20	8	2 for 15	2 for 15	6.6

* Discussed on page 230.

> "You men can't blame us: of two garments of the same quality the women will buy the more expensive; they don't know but *think* it must be better. You wouldn't have us lose that sale to her, would you? She mightn't buy at the lower price because her friend may have paid $70 for her coat and she is suspicious of a $40 coat. Of course, we have to put the price where she'll buy under those circumstances."[1]

It would surprise such a shopper to learn that a woman's silk or wool dress retailing for $39.50 in 1936 cost the manufacturer $12.50 for material and labor. His price to the retailer was $18.75. This spread of $27 is equal to 68 per cent of the retail price.[2] A woman's hat retailing at $5 in 1936 cost $1.71 to manufacture and yielded the manufacturer $2.63 when he sold it to the retailer. This is a spread of $3.29, amounting to 192 per cent of the factory cost and about 66 per cent of the retail price.[3]

Bargaining in the United States. There are some buyers, however, who are shrewd or at least who attempt to fulfill their role as economic men. Instead of being attracted by high prices they delight in bargains; instead of taking quality for granted they attempt to measure it; instead of ordering by telephone they shop around in person. Rather than lose the custom of such buyers, retailers do not hesitate to make price concessions. Instead of taking pride in the high prices they pay, some buyers take pride in never paying the list price marked on the merchandise. To accommodate such customers most department stores have economy basements in which identical, or nearly identical, merchandise is sold at reasonable prices. A Philadelphia department store offered for sale identical dresses priced at $40 on the second floor and $25 in the basement. A Columbus department store sold identical furniture covers for $7.85 on the fourth floor and $2.49 in the basement. When higher-priced merchandise in special departments ceases to move it is sent to the basement for clearance at prices which consumers will pay. Automobiles, refrigerators, washing machines, and many other such commodities carry a nominal retail selling price. Actually that price is what the retailer hopes to get, not the least he will take. Gullible consumers pay it and ask no questions, but shrewd buyers demand and get a price concession. This means that the United States, while nominally a one-price country, is actually a bargaining country. The important difference, however, between the United States and Oriental countries is that in the latter it is

[1] LYND, Robert S. and Helen M., *Middletown*, p. 166, Harcourt, Brace and Company, New York, 1929.

[2] STEWART, Paul W., and DEWHURST, J. Frederic, *Does Distribution Cost Too Much?*, p. 44, The Twentieth Century Fund, New York, 1939. [3] *Ibid.*, p. 42.

common knowledge that bargaining prevails, whereas in the United States it is commonly believed that one price prevails. This operates to the serious disadvantage of those who never bargain, a group which in the United States is probably in the majority.

Price Variations on Identical Merchandise. In the spring of 1933 a study of comparative prices of identical grocery products within and between three markets was undertaken. Prices of 18 nationally advertised products were compared in three Ohio communities. These were Granville, a college village with 1,500 permanent residents and 800 student residents; Bexley, a high-class Columbus suburb; and a residential section in the city of Columbus. Within each market, price quotations were secured from an independent retailer and two chain stores. Results are compiled in Table IV on page 228.[1]

For those who believe in the law of one price the revelations of this study may be surprising, but to those aware of the lack of competition among consumers results will be regarded as typical. In Granville, where the three stores are located on the same street, in the same block, not more than one hundred yards apart, price variations ranging from 9.7 per cent to 80 per cent are found. Although Chain Number 1 and Chain Number 2 prices were frequently the same, not a single one of the eighteen articles was offered for sale at identical prices by the three stores. No one of the stores was consistently lower in price. On six items prices were lower at Chain Number 1, while on seven items prices were lower at Chain Number 2. In most cases independent store prices were higher, but on two items they were lower than either of the other two stores.

Similar analysis yields essentially the same results for Bexley and Columbus.

Two years later a similar study of comparative prices among four stores in Granville revealed striking differences in prices for twelve identical products. In this study price quotations were included for a semi-chain store, in addition to an independent and two chains, as shown in Table V.[2]

Although the greatest distance between these stores is not over one hundred yards, maximum variation in price was 60 per cent for one item, and ranged from 5.2 per cent to 38.8 per cent for all the others. Not a single item was sold at the same price by all stores. Obviously Granville housewives could save on their purchases by shopping around. Part of the variation in price may be explained by the failure of either

[1] Based on a study made by Esther Landrum for the Department of Economics, Denison University, Granville, Ohio, April, 1933. [2] Adapted from Thomas, Elizabeth, *A Comparison of Price for Bulk and Packaged Goods*, an unpublished manuscript on file in the Department of Economics, Denison University.

of the chain stores to provide delivery service or to give credit, yet significant differences will be found between the semi-chain and the independent store, both of which provide both services. In fact their prices are identical on only two of the twelve articles. Although the cash and-carry chain stores should have lowest prices on every article there is not only variation between their prices, but on three items the independent, or the semi-chain, or both, had lower prices than Chain Number 2. For all twelve products Chain Number 1 prices are as low as or lower than those of the other three stores, excepting the price of Chain Number 2 for one item.

TABLE V.—COMPARATIVE PRICES ASKED FOR TWELVE IDENTICAL PRODUCTS BY FOUR RETAILERS IN GRANVILLE, OHIO, IN FEBRUARY, 1935

Product	*Independent*	*Chain No. 1*	*Chain No. 2*	*Semi-chain*	*Maximum Variation*
	cents	*cents*	*cents*	*cents*	*per cent*
Cheese (Kraft, 5 oz. jar)	18	18	21	20	16.6
Coffee (Maxwell House)	35	32	32	37	15.6
Rice (bulk, pound)	8	5	5	7½	60
Macaroni (Fould's, 8 oz.)	10	9	7⅔	9	30.4
Buckwheat Flour (Aunt Jemima)	15	13	13	14	15.4
Crisco	23	20	22	20	15
Vinegar (bulk, gallon)	35	29	29	35	20.7
Lux Soap	3 for 20	3 for 19	3 for 19	3 for 20	5.2
Ivory Soap (large cake)	10	2 for 19	2 for 19	11	15.8
Crystal White Family Soap	5	5 for 18	4 for 17	4½	38.8
Hellman's Blue Ribbon Mayonnaise (pint)	29	29	30	32	10.3
Flour (Gold Medal, 24½ lb.)	1.25	1.15	1.15	1.27	10.4

The Granville price comparison was repeated in June, 1942, the results of which are presented in Table VI. At that time the same stores that were shopped in 1935 were still in operation. The main change that had taken place was the outbreak of war first in Europe and then in the United States, with its resulting price rises. Price control, based on the maximum price charged by each store in the month of March, 1942, had gone into effect May 18. The main conclusion to which the second study leads is that variations in prices for identical merchandise in four stores within 100 yards of each other were as prevalent in 1942 as in 1935. Comparing the maximum percentage variation in the last column, it will be observed that although there are several differences in the extent of variation, variation is still the dominant characteristic. One important difference in the two tables is the lack of price variation on one item—mayonnaise—in 1942. Some curious price changes will be observed. The semi-chain actually charged less for four items than had

been charged in 1935, and the same price for one item. This may be explained by the fact that the store was attempting to meet the competition of chain stores, an attempt which proved unsuccessful, as a result of which the semi-chain went out of business a few months later. It is reported that in this community there was a very large swing to chain stores during the period of rising prices. Although it is not the purpose of this price comparison to show changes over time it is interesting to notice the adjustments in prices which were made by the several stores. As a final comment, it is still accurate to say that Granville housewives could save on their purchases by shopping around.

TABLE VI.—COMPARATIVE PRICES ASKED FOR TWELVE IDENTICAL PRODUCTS BY FOUR RETAILERS IN GRANVILLE, OHIO, IN JUNE, 1942

Product	*Independent*	*Chain No. 1*	*Chain No. 2*	*Semi-Chain*	*Maximum Variation*
	cents	*cents*	*cents*	*cents*	*per cent*
Cheese (Kraft, 5 oz. jar)	19	21	21	19	10.5
Coffee (Maxwell House)	37	36	33	35	12.1
Rice (bulk, pound)	12	2 for 19	10	10	26.3
Macaroni (Fould's, 8 oz.)	10	2 for 19	not stocked	10	5.3
Buckwheat Flour (Aunt Jemima)	13	17	13	15	30.8
Crisco (3 pounds) *	75	73	69	68	10.3
Vinegar (bulk, gallon)	35	25	29	29	40
Lux Toilet Soap	8	3 for 22	3 for 20	7	19.9
Ivory Soap (large cake)	11	11	10	11	10
Crystal White Family Soap	5	6 for 29	4 for 19	5	5.3
Hellman's Blue Ribbon Mayonnaise (pint)	35	35	not stocked	35	0
Flour (Gold Medal, 24 pounds)	1.23	1.21	1.17	1.13	8.8

* This comparison is not perfect since there should be some difference due to the larger size, but it was impossible to get comparable figures for the one-pound size, which was used in 1935.

In the summer of 1938 a price survey was made among grocery stores in Menomonie, Wisconsin, a trading center with a population of 5,000. A three-way comparison was made on 20 nationally advertised items; prices of three independent stores were compared, then prices of three chain stores were compared, and finally a comparison was made of the average prices asked by the three independents in contrast to those quoted by the three chains.

Results of the comparison among independents, all of which provided credit and delivery service, are presented in Table VII. Variations in price on identical merchandise range from a fraction of a cent to 13 cents. In one case the price at one store was 30 per cent higher than at another store. The figures show that for most of the items store number 2 had the lowest price.

TABLE VII.—PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY THREE INDEPENDENT STORES IN MENOMONIE, WISCONSIN, IN JULY, 1938

Nationally Advertised Article	*Store No. 1*	*Store No. 2*	*Store No. 3*	*Maximum Variation*
	cents	*cents*	*cents*	*per cent*
Lux Toilet Soap	3 for 23	3 for 20	3 for 20	15
P and G Soap (large)	6 for 25	10 for 39	Not stocked	6.8
Rinso (med. pkg.)	23	22	23	4.5
Oxydol (med. pkg.)	23	22	23	4.5
Hilex (1 qt.)	23	22	23	4.5
Kellogg's Corn Flakes	12	10	13	30
Quaker Rolled Oats (large Quick)	19	19	20	5.2
Hills Bros. Coffee (1 lb.)	29	27	29	7.4
Hershey's Cocoa (½ lb.)	10	9	10	11.1
Baker's Chocolate (large)	17	15	18	20
Jello	5	5	5	0
Campbell's Soup (Chicken)	12	10	12	20
Heinz Tomato Soup	15	14	Not stocked	7.1
Heinz Beans with Pork (large can)	17	18	15	20
Heinz Catsup (large bottle)	23	20	22	15
Swansdown Cake Flour	28	25	28	12
Yeast Foam	8	8	9	12.5
Kraft Swiss Cheese	23	20	Not stocked	15
One dozen Ball Jars (qt.)	78	72	65	20

TABLE VIII.—PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY THREE INDEPENDENT STORES IN MENOMONIE, WISCONSIN, IN JULY, 1943

Nationally Advertised Article	*Store No. 1*	*Store No. 2*	*Store No. 3*	*Maximum Variation*
	cents	*cents*	*cents*	*per cent*
Lux Toilet Soap	8	3 for 20	8	19.4
P and G Soap (large)	5	3 for 14	5	6.4
Rinso (med. pkg.)	25	23	25	8.7
Oxydol (med. pkg.)	25	23	25	8.7
Hilex (1 qt.)	23	22	23	4.5
Kellogg's Corn Flakes	14	12	13	16.7
Quaker Rolled Oats (large Quick)	27	23	25	17.4
Hills Bros. Coffee (1 lb.)	36	33	35	9.1
Hershey's Cocoa (½ lb.)	13	11	15	36.3
Baker's Chocolate (large)	18	17	19	11.8
Jello	8	7	7	14.3
Campbell's Soup (Chicken)	18	18	19	5.5
Heinz Tomato Soup	15	12	Not stocked	25
Heinz Beans with Pork (large can)	17	16	17	6.2
Heinz Catsup (large bottle)	25	23	Not stocked	8.7
Swansdown Cake Flour	29	27	27	7.4
Yeast Foam	9	8	8	12.5
Kraft Swiss Cheese	25	23	Not stocked	8.7
One dozen Ball Jars (qt.)	75	72	69	8.7

The study of 1938 was repeated in July 1943, with results as shown in Table VIII. Price variations still prevailed, and there was no item for which all stores charged the same price. The percentage variation in prices ranged from a minimum of 4.5 to a maximum of 36.3. Store No. 2 still had the lowest prices on most articles.[1]

Among three cash-and-carry chain stores in 1938 variations were found as shown in Table IX. While all asked 5 cents for Jello there was a 7-cent difference in the maximum and minimum price quotations for Kraft cheese. While there were only two cases of identical prices, there were two items on which price variations exceeded 30 per cent. No one store was consistently lower in price. To get the lowest prices consumers would have to shop around.

TABLE IX.—PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY THREE CHAIN STORES IN MENOMONIE, WISCONSIN, IN JULY, 1938

Nationally Advertised Article	*Store No. 1*	*Store No. 2*	*Store No. 3*	*Maximum Variation*
	cents	*cents*	*cents*	*per cent*
Lux Toilet Soap	3 for 19	3 for 20	4 for 25	6.7
P and G Soap (large)	10 for 39	6 for 25	6 for 25	6.8
Rinso (med. pkg.)	20	22	21	10
Oxydol (med. pkg.)	19	21	21	10.5
Hilex (1 qt.)	22	21	21	4.8
Kellogg's Corn Flakes	10	11½	10	15
Quaker Rolled Oats (large Quick)	18	19	19	5.6
Hills Bros. Coffee (1 lb.)	29	29	27	7.4
Hershey's Cocoa (½ lb.)	9	8	8	12.5
Baker's Chocolate (large)	19	18	17	11.7
Jello	5	5	5	0
Campbell's Soup (Chicken)	9½	11½	10	21
Heinz Tomato Soup	Not stocked	10	13½	35
Heinz Beans with Pork (large can)	14	14	14	0
Heinz Catsup (large bottle)	21	22	19	15.8
Swansdown Cake Flour	23	27	25	17.4
Yeast Foam	8	8	7	14.3
Kraft Swiss Cheese	22	28	21	33.3
One dozen Ball Jars (qt.)	71	69	69	2.9

Comparable figures for July, 1943, are presented in Table X. Instead of two items for which identical prices were charged by all stores, there were six in 1943. The maximum price variation was 23.5 per cent, compared with 35 per cent five years earlier. On all but five items prices had risen, in some cases very substantially.

[1] The figures for Tables VIII, X, and XII were compiled by Miss Natalie Bongey of Stout Institute, Menomonie, Wisconsin.

TABLE X.—PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY THREE CHAIN STORES IN MENOMONIE, WISCONSIN, IN JULY, 1943.

Nationally Advertised Article	*Store No. 1*	*Store No. 2*	*Store No. 3*	*Maximum Variation*
	cents	*cents*	*cents*	*per cent*
Lux Toilet Soap	3 for 20	3 for 20	7	4.5
P and G Soap (large)	3 for 14	3 for 14	3 for 14	0
Rinso (med. pkg.)	23	23	23	0
Oxydol (med. pkg.)	23	23	23	0
Hilex (1 qt.)	17	21	19	23.5
Kellogg's Corn Flakes	12	12	12	0
Quaker Rolled Oats (large Quick)	22	22	22	0
Hills Bros. Coffee (1 lb.)	33	33	33	0
Hershey's Cocoa (½ lb.)	10	11	12	20
Baker's Chocolate (large)	15	17	17	13.3
Jello	6	7	4 for 25	16.7
Campbell's Soup (Chicken)	17	2 for 35	2 for 35	3
Heinz Tomato Soup	11	2 for 27	Not stocked	22.7
Heinz Beans with Pork (large can)	14	Not stocked	Not stocked	0
Heinz Catsup (large bottle)	21	22	21	4.8
Swansdown Cake Flour	29	28	28	3.6
Yeast Foam	2 for 15	8	9	20
Kraft Swiss Cheese	21	20	Not stocked	5
One dozen Ball Jars (qt.)	69	65	69	6.1

In Table XI (page 236) the 1938 price quotations for the three independents and for the three chains have been averaged for purposes of comparison. The latter group undersold the independents on 14 items, their prices were identical on 2 items, and the independents undersold the chains in 3 cases. Obviously an economic buyer seeking the lowest price on all purchases could not deal exclusively with one store, independent or chain.[1]

Comparable figures for July, 1943, are given in Table XII. Average chain store prices are lower than average independent store prices on 18 of the 19 articles. This would seem to suggest that Menomonie consumers should deal with chain stores, but a comparison of Tables VIII and X will reveal that Independent Store No. 2 has a lower price than Chain Store No. 1 on one item and that its prices on several items are the same. It is still true that an economic buyer cannot deal exclusively with one store, independent or chain.

In June, 1942, the same items which had been shopped in Menomonie, Wisconsin, in 1938 were shopped at independent stores and three chain stores in Newark, Ohio. Newark is an industrial city of 35,000,

[1] Based on a study made by Mr. Paul Huber and Mr. Hughitt Moltzau, graduate students at Stout Institute, Menomonie, Wisconsin, July, 1938.

TABLE XI.—AVERAGE PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY INDEPENDENT AND CHAIN STORES IN MENOMONIE, IN JULY, 1938

Nationally Advertised Article	*Independent Stores Average in Cents*	*Chain Stores Average in Cents*	*Variation in Per Cent*
Lux Toilet Soap	7.00	6.41	9.2
P and G Soap (large bar)	4.03	4.07	1
Rinso (medium package)	22.66	21.00	7.9
Oxydol (medium package)	22.66	20.33	11.4
Hilex (1 quart bottle)	22.66	21.33	6.2
Kellogg's Corn Flakes	11.66	10.50	11
Quaker Rolled Oats (large Quick)	19.33	18.66	3.6
Hills Bros. Coffee (1 lb.)	28.33	28.33	0
Hershey's Cocoa (½ lb.)	9.66	8.33	15.9
Baker's Chocolate (large)	16.66	18.00	8
Jello	5.00	5.00	0
Campbell's Soup (Chicken)	11.33	10.33	9.7
Heinz Tomato Soup	14.50	11.75	23.4
Heinz Beans with Pork (large can)	16.66	14.00	19
Heinz Catsup (large bottle)	21.66	20.66	4.8
Swansdown Cake Flour	27.00	25.00	8.0
Yeast Foam	8.33	7.66	8.7
Kraft Swiss Cheese	21.50	23.66	10
One dozen Ball Jars (qt.)	71.66	69.66	2.8

TABLE XII.—AVERAGE PRICES ASKED FOR IDENTICAL GROCERY PRODUCTS BY INDEPENDENT AND CHAIN STORES IN MENOMONIE, IN JULY, 1943

Nationally Advertised Article	*Independent Stores Average in Cents*	*Chain Stores Average in Cents*	*Variation in Per Cent*
Lux Toilet Soap	7.56	6.78	11.7
P and G Soap (large bar)	4.89	4.67	4.7
Rinso (medium package)	24.33	23.00	5.8
Oxydol (medium package)	24.33	23.00	5.8
Hilex (1 quart bottle)	22.67	19.00	19.3
Kellogg's Corn Flakes	13.00	12.00	8.3
Quaker Rolled Oats (large Quick)	25.00	22.00	13.6
Hills Bros. Coffee (1 lb.)	34.67	33.00	5.1
Hershey's Cocoa (½ lb.)	13.00	11.00	18.2
Baker's Chocolate (large)	18.00	16.33	10.8
Jello	7.33	6.41	14.3
Campbell's Soup (Chicken)	18.33	17.33	5.6
Heinz Tomato Soup	13.50	12.25	10.2
Heinz Beans with Pork (large can)	16.67	14.00	11.9
Heinz Catsup (large bottle)	24.00	21.33	12.4
Swansdown Cake Flour	27.67	28.33	2.4
Yeast Foam	8.33	8.17	1.9
Kraft Swiss Cheese	24.00	20.50	17.1
One dozen Ball Jars (qt.)	72.00	67.67	6.5

the population of which was then rising very rapidly with the influx of workers to man the war plants. A perfect comparison was impossible because of differences in brands available in the two communities, but only two items were different. Among the independent stores there was a variation in price ranging from 4.3 to 25 per cent. Among three chain stores prices varied from 1.3 to 21 per cent. Average independent store prices were higher than average chain store prices on 18 of the 19 items for which comparable figures were obtained. The percentage by which average independent store prices exceeded average chain store prices ranged from a minimum of 13.2 to a maximum of 30.

In May, 1943, prices in three stores in Pittsburgh, Pennsylvania, were compared. The items shopped were those needed to meet the food requirements for one week for a family of two adults and two children with an income of $1800 a year. In this case identical items were not shopped, so that the element of quality difference enters as a possible factor in price differences. If all the food had been purchased at Store Number 1 it would have cost $13.18; at Store Number 2 it would have cost $13.66; at Store Number 3, $15.86. If a Pittsburgh housewife were to trade with one store only she would do well to concentrate on Store Number 1, but a study of the figures reveals that Store Number 3 was lower in price on at least three items. In Pittsburgh as in Newark, Granville, Columbus, and Menomonie, the economic buyer must shop around from store to store. The Pittsburgh survey would indicate that by so doing a housewife with $550 to $700 to spend for food could save $140 by taking advantage of price variations. This would represent a saving of from 20 to 25 per cent on the food budget.

The extent of price variations for identical merchandise among stores is illustrated strikingly in the community-price ceilings. Recognizing the general prevalence of higher prices in independent stores, the Office of Price Administration officially allowed them to charge higher prices than could be charged by stores in other price classifications. For example, if a Washington, D. C., housewife purchased one of each of 600 community-priced foods in a small independent store, her bill would be $95; if she made her purchases in an average chain store her bill would be $84; if she went to the supermarket her bill would be only $82.50. An index of price variations for identical merchandise in District of Columbia Food Stores under the Office of Price Administration community-price ceilings is presented in Table XIII. In this table Class I stores are independents whose volume of sales in 1942 was less than $50,000; class II are independents with sales of $50,000 to $250,000; class III are chain stores with sales up to $250,000; class IV comprises any type of store with sales over $250,000. When a commodity (or brand) was not sold in all four types

of stores, its price is not included in Table XIII. Also, such commodities as meat are not included because the independents were under one price system while the chains were under another type.

TABLE XIII.[1]—INDEX OF DISTRICT OF COLUMBIA COMMUNITY PRICES ON FOODS, JUNE, 1943

Volume of Sales	*Class I Independent Stores Under $50,000*	*Class II Ind. Stores $50,000 to $250,000*	*Class III Chain Stores Under $250,000*	*Class IV All Stores Over $250,000*
Canned Baby Foods	100	98	87	84
Bananas	100	100	77	77
Beets (canned)	100	97	87	85
Bread	100	100	100	100
Butter	100	100	95	95
Carrots (canned)	100	98	88	85
Cereals	100	97	85	84
Cheese	100	100	86	86
Coffee	100	100	88	88
Corn (canned)	100	98	85	83
Eggs	100	98	97	95
Flour Mixes	100	100	89	83
Fruit Cocktail (canned)	100	98	85	83
Jellies, Jams, Preserves	100	100	85	85
Lard	100	100	95	92
Lima Beans (canned)	100	98	85	84
Macaroni and Noodles	100	100	98	96
Milk (evaporated, condensed)	100	100	90	90
Packaged Dried Fruit	100	99	83	82
Peas (canned)	100	98	85	84
Peaches (canned)	100	98	85	83
Peanut Butter	100	100	84	84
Pears (canned)	100	99	87	86
Pineapple (canned)	100	94	86	84
Poultry	100	100	99	99
Processed Fish	100	100	82	82
Shortening	100	100	92	92
Sirup	100	100	87	85
Spinach (canned)	100	95	84	84
String Beans (canned)	100	98	86	85
Sugar	100	97	89	88
Tomato Juice (canned)	100	98	86	84
Tomatoes (canned)	100	99	85	84
All Community-Priced Food	100	99	88	87

The St. Paul (Minn.) County Consumers' Council compared eight brands of ice cream, all of which sold for 15 cents a pint. Variations in quality were amazing. Butterfat content varied from 13 to 18 per cent; overrun, that is air content, ranged from 38 to 95 per cent; bacteria count

[1] *Business Week,* June 12, 1943, p. 88.

varied from 5,000 per cubic centimeter to 950,000. These facts assume greater significance when it is realized that some ice creams contain 30 per cent butterfat. Ordinary coffee cream contains 18 per cent. An overrun of 50 per cent means that the ice cream is one third air, while a 100 per cent overrun indicates that the product is half air. Some ice "creams" with an overrun of 130 per cent are more accurately described as iced air. Government specifications for ice cream limit bacteria count to 50,000. A chemist can discover these facts but a buyer has no guide to follow.[1]

Margins and Markups. How does the retailer determine what price to place on his merchandise? According to economic theory the price which he must secure in the long run is that which will just cover total costs of production, not including what economists call pure profit. According to the same theory, if his price is too high consumers will buy elsewhere, thus tending in the long run to an equality in price in the same market. This explanation is true only to the extent that competitive forces operate. To the extent that they do not operate, prices can be above costs of production. The preceding tables illustrate effectively how competitive forces fail to operate.

In practice retail prices are determined in the following manner. To wholesale costs retailers add a markup sufficient to cover their costs of doing business and as much in excess as they think the traffic will bear. Experience has shown many of them that the traffic will bear a considerable burden. In some lines of merchandising, notably necessities, the margin between cost and selling price may be much narrower. Chain grocery stores, for example, operate on the principle of a small margin on a large turnover, a typical markup being 25 per cent. This means that

TABLE XIV.—MARGINS ALLOWED BY OFFICE OF PRICE ADMINISTRATION FOR PERISHABLES AND NON-PERISHABLES, BY STORE SIZE, IN 1943[2]

Class of Store	*Average of Permitted Margins on 16 Non-perishables**	*Average of Permitted Margins on 12 Perishables*
Independents, sales under $20,000	23%	30%
Independents, sales of $20,000 to $49,999	22%	30%
Independents, sales of $50,000 to $249,999	21%	30%
Chains, sales less than $250,000	18%	26%
Any store with sales of $250,000 or more	15%	26%

* Based on net to grocer.

[1] *Consumers' Guide*, June 24, 1935, and July 22, 1935.
[2] *Business Week*, January 30, 1943, p. 18.

an item which retails at $1.00 cost the retailer 80 cents, giving him a margin of 20 cents, or 25 per cent on his cost. Table XIV, on page 239, shows the average of margins permitted by the Office of Price Administration in 1943 for certain perishables and nonperishables, according to size of store.

Jewelry stores, on the other hand, follow the principle of a large margin on a small turnover, a typical markup being 60 to 70 per cent. Wholesale price catalogues for electrical appliances, office supplies, and books regularly quote retailers' prices 50 per cent below the retail price list. To put it another way, if a lamp costs the retailer $5.00, the price which he normally will put on the price tag will be $10.00, equivalent to a markup of 100 per cent. In some cases it may be less and in many cases it may be more. On a necessity such as flour the usual markup is 10 to 35 per cent. Retailers of auto accessories mark up the retail price 40 per cent above cost to them. Comparable figures for retail shoe stores and chain drugstores are 45 and 55 per cent.

In the trade it is customary to figure markup as a percentage of net sales. On that basis jewelry products are marked up from 40 to 50 per cent; electrical appliances, household appliances, hosiery, men's shoes, and radio sets are usually marked up 35 to 40 per cent; tires, auto accessories, rubber shoes, paper products, cosmetics, and fountain pens carry a markup of from 30 to 40 per cent; the margin on oil and gasoline is 25 per cent; the lowest markup is 20 per cent on grocery specialties.[1]

Looking at the problem of marketing costs as a whole, investigators for The Twentieth Century Fund found that the total cost of producing and marketing commodities was 65.6 billion dollars. The marketing costs amounted to 38.5 billion dollars, or 59 per cent of the total. Thus on the average 59 cents out of every dollar spent by consumers goes to those who market the product, while 41 cents goes to those who produce it.[2] In the hundred years 1830 to 1929 the number of people employed in trade and transportation increased ten times compared with the two and a half times increase in the number engaged in manufacturing. This trend continues. Between 1935 and 1940 the total population of the United States increased 3.14 per cent, but the number of retail establishments increased from 1,587,718 to 1,770,904, or 10.35 per cent.[3] What these marketing costs mean to the consumer in the way of prices is shown in Table XV. In the most extreme case 82.5 per cent of the price paid by the consumer-buyer went to those engaged in the marketing of cab-

[1] BORDEN, *op. cit.*, p. 444.

[2] STEWART and DEWHURST, *op. cit.*, p. 117.

[3] MCNAIR, Malcom P., TEELE, Stanley, and MULHEARN, Frances G., *Distribution Costs—An International Digest*, p. 1, Harvard University Graduate School of Business Administration, Boston, 1941.

bages, leaving only 17.5 per cent for the farmer. In all cases except one the percentage of the retail price going to cover marketing costs was over 50, and in all but two cases was over 60.[1]

TABLE XV.—PRICE SPREADS OF UNPROCESSED FOOD PRODUCTS IN 1935[1]

Product	*Price Received by Farmer, Cents*	*Marketing Cost, Cents*	*Retail Price, Cents*	*Price Spread as a Per Cent of Retail Price*
Cabbage (lb.)	.7	3.3	4.0	82.5
Carrots (bunch)	1.0	4.5	5.0	81.8
Celery (bunch)	2.3	8.0	10.3	77.7
Lemons (per doz.)	8.6	18.7	27.3	68.5
Apples (lb.)	1.9	3.9	5.8	67.2
Potatoes	.8	1.1	1.9	57.9
Eggs	24.1	12.5	36.6	34.2

According to the Bureau of Agricultural Economics the farmer's share of the consumer's dollar in 1940 in cents was as follows: eggs 58, potatoes 50, hens 48, dairy products 45, white flour 40, apples 35, onions 31, rice 29, oranges 24, canned tomatoes 17, macaroni 13, soda crackers 9.[2]

Total production costs, covering direct materials, direct labor, and manufacturing overhead are shown in the first column of Table XVI for selected items. Total marketing costs are shown in the second column. In all cases these represent the costs for certain individual firms.

A few specific illustrations of the margin between actual cost of manufacture and retail selling price may serve to indicate how far above production costs retail prices for consumers may go. A standard brand electric refrigerator cost $93.34 to manufacture, but it retailed for $207.50. A large dealer with numerous outlets contracted for a number of the refrigerators at a price of $100 and retailed them for $158. In the first case the marketing costs amounted to $114.16, equal to 55 per cent of the retail price; in the second case marketing costs amounted to $58, equal to 36.7 per cent of the retail price. In this particular case the difference of $49.50 was due mainly to the selling methods used. In the first case numerous salesmen were used with sales managers, block managers, and salesmen receiving commissions ranging from 10 to 15 per cent. Advertising costs amounted to approximately 10 per cent of the retail price. In the second case commissions for salesmen ranged from 4 to 6 per cent and advertising expense was not more than 3 per cent of the retail price.[3]

[1] STEWART and DEWHURST, *op. cit.*, p. 26.

[2] Reprinted by permission from REID, Margaret, *Food for People*, p. 536, published by John Wiley & Sons, New York, 1943.

[3] BORDEN, *op. cit.*, p. 469.

TABLE XVI.—COMPARISON OF PRODUCTION COSTS AND ADVERTISING AND MARKETING COSTS OF CERTAIN MANUFACTURERS AS A PERCENTAGE OF NET SALES[1] (see text on page 241)

Product	*Total Production Costs*	*Total Marketing Costs*
Proprietary Remedy	12.7%	55.4%
Toilet Article	22.6	50.2
Cosmetic	36.1	46.0
Clothing Item	55.4	41.9
Grocery Specialty	30.4	38.9
Fountain Pens	50.4	37.0
Confection	26.6	28.3
Rubber Footwear	72.0	28.3
Tires	75.8	20.1
Household Appliance	78.9	19.2
Hosiery	82.8	12.1
Electrical Appliance	64.1	10.8

According to another study the *average* price paid by consumer-buyers for electric refrigerators in 1935 was $156. Of that sum the cost of manufacture was $58. This is a price spread of $98, $12 of which was retained by the manufacturer, $16 by the wholesaler, and $70 by the retail dealer.[2]

A woman's shoe priced at $5 per pair retail in 1936 cost $2.35 to manufacture. The manufacturer's price to the retailer was $2.92. The spread of $2.65 was equal to 112.8 per cent of the cost and to 53 per cent of the retail price.[3]

A man's hat retailing at $3.50 in 1936 cost the manufacturer $1.70 for materials and labor. His price to the retailer was $2.13. The spread of $1.80 represented 105.9 per cent of factory costs and 51.4 per cent of the retail price.[4]

A large distributor of vacuum cleaners purchased them from a manufacturer for a cash price of $30 each. The distributor's price to the retail buyer was $97.50! Of the $97.50 paid by each buyer $30 went to the manufacturer, $37.50 to the distributor, and $30 to the individual salesman.[5]

A striking illustration of the margin between actual cost to manufacture and retail selling price is to be found in the price ceilings pre-

[1] BORDEN, Neil H., *The Economic Effects of Advertising*, p. 521, Richard D. Irwin, Chicago, 1942. Production costs plus marketing costs do not total 100 per cent because the gross margin available after deducting manufacturing costs from sales income must cover not only marketing costs, but also general administrative costs and profits.

[2] STEWART and DEWHURST, *op. cit.*, p. 52.

[3] *Ibid.*, p. 46.

[4] *Ibid.*, p. 42.

[5] University of Michigan, Conference on Consumer Credit, *Proceedings*, January, 1940, p. 105.

scribed by the Office of Price Administration for pressure cookers. Three companies were authorized to manufacture them and three different prices were set. The highest ceiling price which one manufacturer could charge the jobber was $6.95; the ceiling price from the jobber to the retailer was $9.27; the ceiling price from the retailer to the consumer was $13.90. It will be observed that the price paid by the consumer is exactly double the price received by the manufacturer.[1]

One might conclude that on the basis of such profit margins all retailers would be rich. Obviously this is not the case. As a matter of fact, the number of annual business failures among retail merchandisers runs into thousands. In 1942 out of 9,405 business failures, 5,889 occurred in retail trade. This was 22 per cent smaller than the figures for 1941. In that year out of 11,848 business failures 7,589 occurred in retail trade. This is to be explained chiefly by the fact that most retail merchandising markets are overmanned. In 1933 there were seven retail food stores in the village of Granville. Since then one of the independents has failed and two others have changed hands, while a semi-chain has passed through two receiverships and in 1944 was closed after a third failure. The markups in retail stores reflect in part the costs of the competitive marketing system. In fact, this is one of the most vulnerable points of the economic system and consequently is the point at which consumers' co-operatives are most effective.

In discussing the retail price puzzle *Business Week* raises the question how much markup the traffic will bear. Following the scrapping of N.R.A. codes, retailers decided that the time had come to increase their profits. Driving sharp bargains on wholesale orders, little if any of the saving was passed on to consumers. Although retail prices were raised systematically consumers continued to buy. "The fact that this procedure did not affect sales has whetted appetites for bigger and better markups all along the line." A group of thirteen department stores in 1934 increased their sales 11.3 per cent over 1933 and profits were boosted by 30.2 per cent. Another group of retail stores in 1934 exceeded 1933 sales by 23.4 per cent, while profits increased 45.8 per cent. Three women's apparel chains sold 22.6 per cent more goods in 1934 than in 1933, while their profits were 87 per cent greater.[2] That process was repeated beginning in 1939. Throughout that year, 1940, and 1941, prices were rising and profits were swelling. The process was halted at the retail level with the imposition of price ceilings in May, 1942. An attempt to reverse the process was undertaken by means of subsidy payments in July, 1943, to roll back prices to the level of September, 1942.

[1] *Business Week,* June 5, 1943.

[2] *Business Week,* September 14, 1935, p. 8.

What Is in a Can? When consumers shop for merchandise the standards by which they attempt to measure quality in relation to price are a strange and fearful mixture of their own experience, tips from friends, advertising, slogans, brands, trade-marks, labels, and salesmanship. There is probably no other merchandise concerning which consumers are so completely in the dark as canned goods. Here of necessity the buyer relies on price as a measure of quality. This is particularly true when previous experience with a cheap product has been unsatisfactory. Retail merchandisers of canned goods can easily capitalize consumer ignorance by the simple process of raising prices. Without a word of misrepresentation on the part of sellers many consumers will conclude that high price is an indication of quality. As a result "price has become even less of a guide to quality than it was formerly. In fact for many articles there may be little relation between quality and price."[1] According to one account, fruit marketed by the California Fruit Growers Exchange under the brand name Sunkist sold for 43.5 cents more a box than other fruit physically identical with it but sold by less well-organized marketing agencies.[2]

A group of housewives conducted an experiment to determine what relation, if any, there was between quality and price of canned goods. Among several different stores they purchased 150 cans of peas, corn, and tomatoes representing 19 different brands. Their main conclusion was that price is a very poor guide for quality. Of the 150 cans 47 contained peas. The very best can cost 13½ cents per pound of contents, as compared with 20 cents for the most expensive and 8 cents for the cheapest. Of the highest-priced cans costing from 17½ to 20 cents per pound of contents not one was given an A grading. Three were graded B and four C. In the price range from 15 to 17½ cents four cans graded B, while seven graded C. The price range from 12½ to 15 cents contained the only grade A peas in the entire lot. A higher price was paid for twenty other cans grading B or C, yet the brand mark proved meaningless, for of three cans of the same brand one graded A, one B, and one C. Of the fourteen cans in this price range one graded A, eight B, three C, and two below C. The lowest price range included cans selling for 12½

[1] United States Department of the Interior, Office of Education, *Consumer-Buying in the Educational Program for Homemaking*, Vocational Education Bulletin, No. 182, p. 6, Washington, D. C., 1935.

[2] O'Brien, Ruth, and Hartley, Olive, *An Analysis of Consumers' Facilities for Judging Merchandise*, an excerpt from the Report of the Subcommittee on Purchasing Procedures of the Committee on Household Management of the President's Conference on Home Building and Home Ownership, December, 1931. Mimeographed by the American Association of University Women, Washington, D. C.

cents or less per pound of contents. Of the fifteen cans in this group one graded B, six C, and eight below C. While it is true that most cans grading below C were in the lowest price group it is also true that two cans grading below C were in the next highest price group, while one can grading B was in the lowest price group. In the price range 12½ to 15 cents four cans graded C, while in the price group below 12½ cents per pound six cans graded C.

Label indications were altogether useless as a guide. Such terms as First Class, Excellent, Selected, or Best included peas grading from B to below C. Of six cans marked Fancy, four graded B and two C.

Brands were a little more helpful, but not reliable. Three cans of one brand graded uniformly B, while five cans of another brand were all below C. Four cans of a third brand graded A, B, B, C.[1]

In one winter (in normal times), inspectors for the Food and Drug Administration purchased 505 cans of fruit and vegetables in Washington, New York, Philadelphia, Chicago, St. Louis, and New Orleans. From six to twelve stores of varying types were patronized in each city. Purchases were confined to No. 2 cans of vegetables, and No. 2½ cans of fruit. Contents were tested and graded. The following table reveals in a striking way price variations within and between grades.

TABLE XVII.—PRICE VARIATIONS WITHIN AND BETWEEN GRADES OF 505 CANS OF FRUITS AND VEGETABLES

Product	*Grade A Price Range*	*Grade B Price Range*	*Grade C Price Range*	*Substandard Price Range*
Peaches, No. 2½ cans	17–35¢	15–28¢	14–24¢	10–15¢
Tomatoes, No. 2 cans	9–19¢	7–18¢	7–15¢	7–13¢
Corn, No. 2 cans	10–23¢	10–13¢	9–20¢	9–10¢

Some buyers, for instance, were paying as much for substandard peaches as others were paying for grade B and more than the price for which grade C could be purchased. The price range within grade A is over 100 per cent for peaches, tomatoes, and corn. Some of this variation is explained by the practice of jobbers who order 1,000 cases of a single-grade fruit or vegetable. These cases are then broken up, some of them, perhaps half of the lot, being labeled Fancy and marked 25 cents, one quarter of the lot being labeled Choice and priced at 16 cents, while the remainder are labeled as Standard to be sold at 12½ cents.[2]

A similar study, by agencies representing the County Consumers Council, the American Home Economics Association, and various

[1] *Consumers' Guide*, July 9, 1934, p. 6.

[2] LAMB, Ruth de Forest, *American Chamber of Horrors*, p. 176.

departments of the Federal government, was made of 832 cans of fruit and vegetables purchased at retail in seven large cities. Every sample was graded by methods used in the Department of Agriculture. Grades A, B, C, and SS, corresponding to "Fancy," "Choice," "Standard," and "Substandard," were used. Results of the test are shown in Table XVIII.

TABLE XVIII.—PRICE VARIATIONS WITHIN AND BETWEEN GRADES OF 832 CANS OF FRUITS AND VEGETABLES

Product	*Grade*	*Price Range in Cents*	*Product*	*Grade*	*Price Range in Cents*
Beans, green and wax; number of tests, 39	A	12–25	Peas; number of tests, 68	A	10–15
	B	8–18		B	10–20
	C	7–18		C	9–25
	SS	7–12		SS	8–13
Beans, Lima; number of tests, 32	A	8–17	Tomatoes; number of tests, 220	A	7–13
	B	7–18		B	6–15
	C	8–17		C	6–13
	SS	0		SS	6–11
Corn, cream style; number of tests, 244	A	8–18	Peaches, clingstone; number of tests, 179	A	9–19
	B	8–18		B	8–16
	C	7–16		C	7–13
	SS	7–10		SS	7–12
Corn, grain style; number of tests, 23	A	12	Pears, Bartlett; number of tests, 27	A	11–20
	B	8–19		B	10–20
	C	11–16		C	8–20
	SS	0		SS	0

One fact which stands out strikingly is that consumers could buy a can of grade A peas for 10 cents or, if they followed price as a guide to quality, they might pay 25 cents for a can of grade C peas. This is perhaps the most extreme variation, but the entire test revealed the complete ineffectiveness of price as a guide. In several cases the price range for products of identical grade is over 100 per cent.[1]

The New Jersey Department of Agriculture, Division of Consumer Information, tells consumers that they cannot judge the quality of canned goods by the price. Results of their tests of sample lots of tomatoes, peas, and peaches were quite similar to those already given. Although most of the peas, in No. 2 cans, were of good quality, prices for grade A cans varied from 15 to 23 cents; and one can scoring as grade B cost 19 cents, 4 cents more than the price for a can of grade A product.[2]

The State Food Commissioner and Chemist of North Dakota ana-

[1] The Consumers' Division, National Recovery Administration, *The Consumer*, November 1, 1935, p. A.

[2] *Consumers' Guide*, June 15, 1936.

lyzed forty cans of asparagus tips. Of that number 8 were graded A, none B, 23 C, and 9 D. The minimum price per pound for the grade A product was 18 cents, the maximum 37; the minimum for grade C 21, the maximum 37; the minimum for grade D 18, the maximum 35.[1] Many other illustrations of this type of price variation are to be found in the North Dakota report. Most of the packers made no claims as to the quality of their product, but the one packer who claimed grade A actually supplied grade A quality and his price was 18 cents per pound. Nine packers whose products tested grade C claimed on their labels that they were Fancy. And two packers whose products graded D also claimed that the contents were Fancy. Obviously price bore no relation to quality. One could pay 18 cents for grade A or grade B, or one could pay 37 cents for grade A or grade C.

Considerable evidence has been presented and more is available to show that there is little relation between price and quantity or quality of canned fruits and vegetables. There are about 4,500 brands of canned corn, 1,000 brands of canned peaches, and 1,000 brands of canned salmon. It costs but little to design and register a brand. From the consumer point of view even that small cost is of doubtful validity in view of the evidence that brand names are in no sense a guide to quality or quantity.

What Does a Gas Pump Hold? Owners of 32,000,000 automobiles depend on privately owned and operated oil companies to supply them with good quality gasoline at a fair price. Gasoline is a product which results from a highly technical refining process. Probably no individual consumer has the technical ability or equipment for testing the quality of gasoline. This means that most buyers are completely dependent on price as a guide to quality. Gasoline refiners have sought with the aid of advertising to develop a consumer conviction of the superiority of their particular product. In this they have been successful to a high degree. One buyer is convinced that gasoline sold by the Standard Oil Company is the best, while another will use only that gasoline carrying the name of Pure Oil, or Sinclair, or Shell, or one of a host of other brands. This, in spite of the fact that a recent local survey revealed that three nationally advertised brands of gasoline all came from the same vat in a near-by refinery.

In 1936 the price of gasoline at a Gulf port was 5½ cents; the tank car price at New York was 6½ cents; the margin to the jobber was 2 cents; the margin to the retailer, 4 cents; the retail filling station price, 12½ cents; state and Federal tax 5 cents, for a total of 17½ cents retail price.

[1] State Laboratories Department, *Bulletin No. 67*, pp. 68–71, Bismarck, North Dakota, June 1942.

The excessive number of filling stations with a consequent low average volume of sales is a factor in the high cost of marketing gasoline. Stewart and Dewhurst estimate that if the number of filling stations were cut in two their customers would still be adequately served, the volume per station would be doubled, and the unit cost of selling could be reduced greatly.[1]

When an untutored buyer pulls up to a gasoline pump, the forces lying back of his decision to purchase that particular gasoline represent a combination of faith and hope. In a given market, price ceases to operate as a guide because in most cases standard brands are sold at identical prices. Surveys in Granville, Ohio, and Menomonie, Wisconsin, revealed identical prices per gallon for all grades of seven nationally advertised gasolines. Some consumers are influenced by color, unaware that coloring is considered of no value as a measure of quality. As a result of their professional training some buyers know the meaning and significance of such terms as octane rating or vapor lock. They may be aware of the dangers of oil dilution, corrosion, or presence of gum, but usually have no way of testing gasolines for these properties, and no gasoline company has so far presented any reliable information either through its advertising or through its salesmen. The average filling station attendant is uninformed on the technical information concerning the products themselves. His decision to handle a particular brand is reached on the basis of other factors, such as the margin he can secure.

Some years ago the demand for gasoline was comparatively small and the process of securing it comparatively simple. Crude petroleum was heated to its boiling point, vapors being passed off through condensing pipes. Gasoline was skimmed off the top and called "straight run." Increasing use of automobiles and declining use of kerosene for lamps and cooking revolutionized the refining process. By a process known as cracking, greater heat is applied to crude petroleum, resulting in a larger proportion of gasoline. Today nearly half of the crude petroleum thus refined may be converted into gasoline. The octane rating of gasoline is a number which indicates its antiknock qualities. If the octane rating is low the gasoline will cause a motor to knock, while a high octane rating eliminates knocking to a large extent. The octane number is no longer as useful a guide to quality since it has been discovered that addition of lead will reduce the tendency of gasoline to create a knock. This knock is created by the rapid burning of gasoline, resulting in sudden expansion of piston head and cylinder walls. A moderate knock is not only not serious but may actually indicate efficient

[1] STEWART and DEWHURST, *op. cit.*, pp. 55, 56.

operation of the motor. Severe knocking is, however, likely to cause damage.

As engineers have increased the compression of modern motors the tendency of ordinary gasoline to create a knock has been increased. This led motor fuel engineers to step up the octane rating. Whereas some fuels formerly rated 40, third-grade gasolines now run from 60 to 63, straight run gasoline from 68 to 70, while premium gasolines containing lead range from 76 to 80. The process of adding lead to gasoline is patented by the Ethyl Gasoline Corporation. Refiners may secure the right to use this process only by license which is issued on condition that a 2-cent margin be maintained over standard gasoline prices. The stock of this corporation is owned by General Motors and Standard Oil of New Jersey.

Although modern high compression motors operate more smoothly on a high octane gas they will operate quite satisfactorily on a regular grade and in many cases a third-grade gasoline will yield satisfactory results. There is only one chance in ten that a third-grade gasoline will contain any harmful ingredients such as sulphur or gum. So far as mileage is concerned in relation to cost there is very little difference between premium, regular, or third-grade gasoline. Any gasoline which will operate the motor satisfactorily will yield good mileage. All gasolines have practically the same heat value and the average motor converts only 10 per cent or less of this heat energy into power at the rear wheels.

While there is a great variation in quality of crude petroleum, modern refining processes have become so standardized that gasoline is fairly uniform in quality no matter from what oil or refinery it comes. The practice of swapping gasolines behind the scenes has become rather general among the major companies. In order to save transportation costs gasoline will be taken from the nearest refinery and poured into an underground storage tank from which it will be delivered to the consumer's car through a brightly colored pump bearing a widely advertised trade name. In that mesmeric process the only change which has taken place is that in the buyer's mind. Straight run, identical bulk gasoline has become to him through the process of advertising a distinctive, marvelous motor fuel which costs more because it is worth it.

The major companies normally supply about 80 per cent of their own needs, purchasing the remainder of their supply from independent companies. An independent retailer on the other hand may purchase branded gasoline from a major company and sell it as an unbranded product or he may purchase an unbranded product of low grade and attempt to sell it as premium gasoline. The net result is that a buyer has absolutely no guide as he weaves his way among the labyrinth of gasoline

pumps. Neither price, nor color, nor brand name offers any assurance of quality.[1]

Have You Changed Your Oil Recently? One of the most needless of modern wastes has been encouraged deliberately by oil companies. Through advertising and salesmanship consumers have been told that they should change their motor oil periodically. At one time they were told to change every 500 miles. Since then the figure has been raised to 1,000, 1,500, and 2,000 miles. One oil company is now advertising a 2,000-mile oil, but in the opinion of many competent lubrication engineers neither that nor any other oil need ever be changed. In the process of lubricating a motor only two things can happen to oil. Any sediment which is sufficiently heavy to cause damage to a motor will settle to the bottom of the crankcase. Any other foreign substance will dissolve in the oil and become harmless. All that is needed is to add sufficient oil to keep the motor properly lubricated. Owners of large fleets of cars salvage all oil, recondition, and use it again. Individual owners may safely operate their automobiles year after year, changing the oil only with the change in seasons. In September, 1942, all operators of automobiles owned by and operated for the Federal government were ordered by the Director of the Bureau of the Budget to change motor oil only twice yearly in the future—in the spring and in the fall. It was estimated that that order would save 750,000 gallons of oil, formerly wasted.[2]

A far more plausible reason for changing oil is that of varying the type according to weather. Yet oil companies have not featured this in their advertising. Effective operating results may be secured by two changes a year. In the spring the crankcase may be drained and filled with summer oil and in the fall the summer oil replaced with winter oil.

As in the case of gasoline, there is no relation between color and price. Light colors and transparency are obtained by the refining process. Nor is price an indication of quality. The United States government buys motor oil on specification at 28 cents a gallon. For oil which is certainly no better the individual consumer pays $1.00 to $1.40 per gallon. The purchasing agent for Hamilton County, Ohio, testified before the Temporary National Economic Committee that he purchased automotive lubricating oil on specification for the city of Cincinnati at a price of 33 cents a gallon. The same oil, according to his testimony, was sold at retail priced at 35 cents a quart—$1.40 per gallon.[3] After making ade-

[1] *The Consumer*, "What Is Gasoline?", November 1, 1935, pp. 12–16. Household Finance Corporation, *Better Buymanship*, Bulletin No. 13. State Food Commissioner and Chemist, *Bulletin No. 68: Petroleum Products*, Bismarck, North Dakota, August, 1942.

[2] *The Ohio Cooperator*, September, 1942.

[3] Temporary National Economic Committee, *Hearings*, Part 8, *Problems of the Consumer*, p. 3445, United States Government Printing Office, Washington, 1939.

quate allowance for the economy of large-scale buying this margin is still too great. Individual buyers may pay 35 cents a quart if they wish, but they can secure a satisfactory oil for 10 to 15 cents a quart. According to lubrication engineers there is very little oil offered on the market which is so poor in quality that it can possibly damage a motor. There is only one essential and that is to keep the crankcase well filled.[1]

What Is a Tire? In 1926 Sears, Roebuck & Company made a three-year contract whereby Goodyear Tire and Rubber Company was to fulfill all tire requirements for the mail order firm. The price was to be cost of manufacture plus a profit of six per cent, later adjusted to six and one-half per cent. The Sears company was to do its own advertising and to sell the tires under its own trade name. In May, 1928, a second contract was signed covering requirements to December 31, 1932. In the summer of 1931 Sears, threatening to terminate the contract, succeeded in getting a new agreement for ten years under which the Goodyear company agreed to pay Sears an unnamed sum in cash, and common stock to the amount of $1,250,000. The contract called for a price of costs plus profits. Under these contracts Goodyear manufactured and sold to Sears in the eight years 1926–1933 more than 19,000,000 tires, for which Sears paid $129,250,984 gross and $116,359,367 net. Goodyear made a total net profit on the Sears contract of $7,715,794.56 according to evidence presented before the Federal Trade Commission. On sales of equal volume to service station dealers Goodyear made a net profit of $20,420,807.21. The difference of $12,710,012.65 was held by the Commission to be a price discrimination not accounted for by differences in cost, transportation, and selling. The case was appealed to the Circuit Court of Appeals and in his opinion Circuit Judge Hamilton said, "The Commission finds, and the undisputed evidence shows, there was no difference in grade or quality between the tires petitioner sold to its dealers generally and those sold to Sears, Roebuck & Company. . . ."[2] The 1930 retail price for Goodyear All Weather Tires was $8.40. The total distribution cost was $3.44, equal to 41 per cent of the retail price. Sears, Roebuck All State Tires, equal in grade and quality according to the Federal Trade Commission, retailed for $6.47 if purchased at the stores and for $6.17 if purchased by mail. The store price represented a distribution cost of $2.07, equal to 30.2 per cent of the retail price. Purchased under identical conditions the identical tire would cost the Sears customer $1.93 less than the Goodyear customer.[3]

During the investigation an official of the rubber company contended

[1] *Better Buymanship*, Bulletin No. 13.
[2] Federal Trade Commission, *Decisions*, Vol. 28, pp. 1899–1912, February 16, 1939.
[3] Stewart and Dewhurst, *op. cit.*, p. 54.

that there is no such thing as an abstract standard of quality for tires. According to his statement there is no such thing as a first-line tire. Some manufacturers make third-line tires and sell them as firsts. The only test according to that official is performance, in which there is a variability of 300 per cent. Yet his company spent $72,000,000 advertising the virtues of its tires to buyers.[1]

What's in a Name? Modern merchandising is based very largely on the practice of creating in consumer minds an association of quality with a particular trade name. By the repetitive method of advertising, consumers are told that a certain name stands for quality, but rarely if ever are they given any factual evidence. Preceding illustrations have shown how meaningless trade names may be on cans, gas pumps, motor oils, and tires. Several additional illustrations chosen at random will fortify the conclusion that consumers cannot rely on private trade names as a guide to quality. Neither can they rely on their own judgment or on price. As a result they are engaged in a game of blindman's buff in which they usually pay a fancy price for the privilege of playing.

A three-way test for sheeting shows that once a sheet leaves a factory the only reliable test of quality is that conducted in a laboratory by properly qualified technicians. The consumer cannot judge quality by observation or touch, neither can she judge quality by comparing prices; nor can she rely on salespeople for guidance. Under direction of Professor Rosamond C. Cook, nine brands of sheets were tested scientifically in a laboratory. Results showed a confusing lack of correlation between quality and price. The best quality sheet was lower in price than three others of an inferior grade. On the other hand, the most expensive sheet ranked third in quality. The cheapest sample graded sixth in quality, better than three others whose prices were higher. The brand ranking eighth in quality was second highest in price. Two sheets were of identical quality, yet one was priced two and one-half times as high as the other.

After having set a definite laboratory standard the sheets were then shown to a group of consumers who were asked to judge them as to quality, all price tags having been removed. The only sample on which consumer judges agreed with the laboratory tests was on that sheet which ranked lowest in quality. The one which they ranked highest in quality was actually fourth in the laboratory tests, while that graded second by consumers was actually seventh.

As the third step in this experiment salespeople in two of the best retail stores in New York were asked to judge the quality of the nine sheets. These people had been given special training in textiles, yet their judgment, taking the laboratory test as a standard, showed them no

[1] *The Consumer*, vol. 1, No. 2, p. 2.

more capable than consumers in judging quality. According to their judgment the sheets ranking first and fourth were tied in fifth position. Their judgment was correct only on the two poorest samples.

As a final step in the test, analysis of advertising for these nine sheets was made. For one brand alone was there any sort of definite statement. All other statements were general or so obvious as to be useless in providing prospective buyers with any information as to quality.[1]

Towels, like sheets, are difficult to judge. What the consumer wants is a sturdy, well-made product at a reasonable price. These qualities depend on materials used and methods of manufacture, such as the number of threads per inch. Unless the label gives such information the average buyer has no other way of securing it. So again she turns to price as a guide. In this case one source of information holds that towels priced up to $1.25 usually bear a fairly close relationship to size and quality. Above that price anything which consumers pay is mostly for style or extra profit. To prove that advertised brands are the best profit-makers the manufacturers of Cannon Towels conducted a sales test. Cannon Towels were placed side by side with unbranded towels, identical as to quality. Although the branded towels were priced 10 per cent higher than the unbranded ones they outsold the unbranded towels at the rate of 3.6 to 1. These results were confirmed in tests in seven different cities.[2]

Millions of consumers require many more millions of hose and shoes each year. Admitting their inability to judge quality of either of these products, to what extent can they rely on price as a measure of quality? Tests of hosiery conducted by the Industrial By-Products and Research Corporation of Philadelphia and by the National Bureau of Standards led to the conclusion that there is little relation between price and quality. The silk heels of a pair of stockings priced at 59 cents wore 50 per cent longer than those of a pair priced at $1.15, even though both had the same thread count. The heels of another pair of hose priced at $1.00 lasted twice as long on the abrasion machine as a pair selling for $1.35. Stockings of inferior quality may be wrapped in a pretty cellophane package and priced at $1.35.[3]

Purchasing shoes is not unlike purchasing canned products. While it is true that the buyer sees his shoes there are so many things he does not see that he is wholly incapable of judging quality. Modern practitioners of fraud are clever enough to make brown paper look and smell like

[1] A pamphlet describing the test may be secured from Professor Rosamond C. Cook, University of Cincinnati.

[2] Williams, F. A., "Advertised Brands Prove To Be Best Profit Makers," in *Printers' Ink*, p. 3, September 29, 1932, quoted in Borden, *op. cit.*, p. 604.

[3] *Better Buymanship*, Bulletin No. 4; Temporary National Economic Committee *Consumer Standards*, Monograph No. 24, p. 89.

leather. In buying shoes the consumer is influenced chiefly by price, appearance, and comfort. Inferior products can be made to look attractive and a shoe can be manipulated so as to make it feel comfortable. If then the buyer pays a fancy price he has done his best to make an intelligent selection. At one time shoe merchants used a standard markup of 40 per cent on all shoes. But times have changed. The markup now ranges from 20 to 50 per cent. Shoes bearing identical price tags may vary considerably in quality. One pair may have a better upper but inferior materials or construction elsewhere. Each shoe width requires a separate pattern, but many manufacturers cut several widths by the same pattern, later shaping them on the lasting form. Of course, this results in low quality shoes. According to one authority as much as 30 per cent of leather used for shoe manufacturing is not suited for good shoes. For example, hides of animals exposed to drought make inferior leather.[1]

The manner in which modern producers run cheap silks through baths of mineral salts to give them added weight has already been mentioned. When a consumer proceeds to buy silk goods it is difficult if not impossible to distinguish between genuine silk and the weighted product. Having no other guide to which she may turn, the average buyer relies on price. But unfortunately price is no more accurate as a guide in buying silks than in buying any other product. "The fabric in a $30 dress may be no better than one in a $15 dress." Price differences may be based on exclusive design, better workmanship, or merely a larger margin for the seller.[2]

In purchasing carpets and rugs "price cannot be relied upon to indicate comparative differences in durability." The pile of a rug selling for $5.25 a square yard wore down after 75,000 revolutions of a testing machine, while the pile of a rug selling for $6.85 lasted 300,000 revolutions. For a 30 per cent additional investment a buyer could secure a 300 per cent greater durability. The secret of durability lies in the density of the pile. In this case the better rug had 12 per cent more pile tufts.[3]

For many other products it is doubtless true that a slightly increased expenditure for quality would yield far more than proportionate returns in durability. Automobile engineers calculate that for 15 to 30 per cent greater cost the life of a car could be increased from the present limit of about 50,000 miles to 250,000 or 500,000 miles.

Oriental rugs provide an illustration of the false standards by which consumers judge quality, and of the way producers cater to such ideas. American buyers insist on a rug with brilliant sheen-like finish. To meet that demand producers of these rugs subject them to a severe chemical

[1] *Better Buymanship*, Bulletin No. 4.
[2] *Ibid.*, Bulletin No. 5.
[3] *Ibid.*, Bulletin No. 10.

scrubbing. Although that process reduces their serviceability by 25 years, it is commonly used to meet consumer demand.

Turning to soaps, we find the same lack of standards by which consumers can judge quality. Under the present marketing system women buyers have no way of determining how much real soap they are getting in bars or packages. At one time soap chips contained as much as 85 per cent real soap and laundry bars contained up to 60 per cent of soap. Since then price competition has resulted in increasing use of filler and water. "While the consumer may be blamed for creating a demand for larger packages containing a constantly decreasing percentage of soap, it must be conceded that consumer demand is an artificial creature sired by advertising and merchandising practice. . . . "[1]

According to Borden, competition has been quite ineffective in the merchandising of drugs, toilet goods, and cosmetics. Competitive advertising and aggressive selling have been intense, while the margins between manufacturing costs and selling prices have been the greatest. Consumers have lacked any basis for judging the quality of such products. It is not even possible to judge them on the basis of their performance in use. In fact the satisfaction which one gets from using them may be in part a result of ideas which have been given by advertising. Knowing that some drugs are or may be dangerous, one writer thinks that consumers have been willing to pay a high price for brand familiarity. What this really means is that in the absence of any standards for quality and in the absence of grade labeling consumer-buyers have necessarily fallen back upon the assertions of the merchandisers.[2] The results of this situation are revealed in the following figures. Our per capita expenditure for drugs in 1929 was $6.00. At that time an Army post supplied necessary drugs at the rate of 72 cents per capita, while an industrial concern did the job for $1.18. The difference between the prices paid by or for soldiers and workers on the one hand and consumer-buyers on the other reflects the margin which the latter group pays for proprietary drugs with trade names. "A group of a dozen proprietary drugs was found to average $25.30 per ounce in cost whereas the identical group could be bought under their proper chemical name for $6.40 an ounce, hence consumers pay $18.90 an ounce simply to get a trade name on it. Our drug bill is at present at least $450,000,000 a year higher than it needs to be."[3] In June, 1938, Bayer's Aspirin was being sold at wholesale at a price of 75 cents an ounce; "at the same time aspirin under its generic term of

[1] "Oil and Soap," a publication of the American Oil Chemists Society, quoted from *Better Buymanship*, Bulletin No. 16.

[2] BORDEN, *op. cit.*, p. 604.

[3] HARDING, T. Swann, "Doctors Deserve a Better Deal," in *The Christian Century*, April 30, 1941, p. 593.

acetyl salicylic acid was available at wholesale at 13 cents an ounce. . . ."[1] The retail price for Bayer's Aspirin is 59 cents a hundred tablets, for Squibb's 39 cents, and for Macy's 18 cents, yet all of these are required to conform to the United States Pharmacopoeia or the National Formulary. The purchasing agent for Hamilton County, Ohio, is able to buy unbranded aspirin at a price of five cents a hundred.

Despite the fact that there are over 500 firms manufacturing dentifrices and that there are something over 700 different brands the amount of competition in that field is relatively small. It has been estimated that 90 per cent of the market is dominated by ten advertised brands. The comparative prices per ounce for nineteen brands in retail stores in Boston are shown in Table XIX. In general these figures show that the widely advertised brands cost considerably more per ounce than the unadvertised, such as Craig-Martin. On the March 1, 1941, list of dentifrices approved by the Council on Dental Therapeutics of the American Dental Association, Kolynos, Pepsodent, Craig-Martin, and Sears were the only four included out of the nineteen listed in the foregoing table. This would indicate that a consumer-buyer could get a satisfactory dentifrice for 3.6 cents an ounce, or he could pay 18.5 cents an ounce for one no better or no worse. Without the aid of the American Dental Association most buyers would be inclined to "play safe" by paying 18.5 cents.

TABLE XIX.—COMPARATIVE PRICES PER OUNCE OF NINETEEN BRANDS OF DENTIFRICES IN BOSTON STORES, FEBRUARY, 1941[2]

Brand	*Price per Ounce*	*Brand*	*Price per Ounce*
Bost	\$0.133	Pepsodent	\$0.12
Briten (United Drug)	0.087	Phillips	0.10
Colgate	0.11	Rexall Milk of Mag. (United Drug)	0.088
Iodent	0.11	Squibb	0.11
Ipana	0.15	St. 37	0.131
Kolynos	0.185	Worcester	0.103
Klenzo (United Drug)	0.111	Craig-Martin (Woolworth)	0.036
Listerine	0.08	Sears (Sears, Roebuck & Co.)	0.096
Mi. (United Drug)	0.095	Approved Milk of Mag. (Sears, Roebuck & Co.)	
Pebeco	0.12		0.057

There is probably no field of merchandising in which consumers' propensity to follow price as a guide to quality has been more highly capitalized than in selling cosmetics. Borden relates the experience of a department store which carried high grade cosmetics under its own

[1] BORDEN, Neil H., *op. cit.*, *The Economic Effects of Advertising*, p. 576, Richard D. Irwin, Chicago, 1942.

[2] BORDEN, *op. cit.*, p. 556.

brand name, offering them at prices considerably below the prices asked for well-known brands. But even with wide price differentials, sales for the higher-priced advertised brands greatly exceeded the sales of the store's own brand. As a result the store raised its prices to a point slightly below those of several of the leading brands and then in its advertising made quality comparisons. The result was a substantial increase in sales.[1] Samples of cosmetics were purchased in drug stores, department stores, and five-and-ten-cent stores and then analyzed in a commercial laboratory. The results showed little relationship between cosmetic quality and price. One brand priced at 47 cents an ounce was graded highest in quality; the one which was priced the highest, 61 cents an ounce, was no better. In fact there was little choice between the 18-cent and the 61-cent brands. Four brands of cleansing cream proved to be almost identical in composition, yet their prices ranged from 15 to 58 cents. One brand of lipstick at $1.00 an ounce was fully as good as another brand costing $7.00 an ounce.[2]

It is not at all necessary to pay a high price to obtain good cosmetics. Many products selling at low prices contain high quality, pure ingredients, and are skillfully blended.[3] Manufacturers of paraffin and petrolatum blends manufacture the basic cream for face cream by the ton. Except for differences in perfuming and packaging all of the creams might come from the same batch. In fact, one manufacturer was found to be packaging his cold cream under one label for a five-and-ten-cent store and the identical cream was being packaged for a beauty salon to be sold under its label in slightly larger and more elaborate jars at a price of $6.00 a jar.[4] But the consumer has absolutely no way of ascertaining what ingredients are used. A face powder selling for $3.00 costs 23 cents for ingredients and 16 cents for container; a perfume selling at $2.75 costs 26 cents for ingredients and one cent for the container; an astringent consisting of a small amount of alum in alcohol and water selling at $1.75 costs 8.5 cents for ingredients and .5 cents for container.[5] No effort has been made to establish a basis on which a buyer can measure effectiveness in relation to price. Ingredients are but a small part of the cost for any cosmetic. Packaging, advertising, and profits swell the price. Talc for face powder costs $60 to $80 a ton. Mrs. Helen Woodward describes the way in which she and her associates established Primrose

[1] BORDEN, *op. cit.*, pp. 582, 583. [2] MILLER, Lois Mattox, "Cosmetic Comedy," *op. cit.*, p. 19. For detailed price comparisons on dusting powders, face powders, lipsticks, rouge, and astringents, see Temporary National Economic Committee, *Problems of the Consumer*, pp. 33, 34. [3] *Better Buymanship*, Bulletin, No. 12, p. 4. [4] MILLER, "Cosmetic Comedy," *op. cit.*, pp. 19, 20.

[5] SOLOMON, *The Traffic in Health*, *op. cit.*, pp. 329–331. For additional comparisons see BORDEN, *The Economic Effects of Advertising*, pp. 580–581.

House, deliberately designed to capitalize consumer ignorance and snobbishness:

"There are, unfortunately, many men and women who will not buy anything unless it is high-priced; who select their clothes by the label of the maker; who feel that they gain something by having on their dressing tables the same jars and bottles that stand on the tables of Mrs. Vanderbilt, Mrs. Astor, or some other newspaper society star."[1]

The financial backers of Primrose House set out to give consumers an opportunity to pay fancy prices. Appeal to snobbishness was made by using the name of a society leader. There are two types of concerns in the cosmetic trade. One sells its products at a low price in large quantities through drug and department stores. The other follows a much more subtle and indirect procedure. These companies concoct a large number of creams, powders, and lotions at high prices. They operate in an atmosphere of elegance and illusion—an illusion which enables them to add from 500 to 1,000 per cent to their costs.

For one final illustration let us turn to a commercial source:

"The two sales appeals most frequently used in selling electric shavers are price, if the price is attractive; or, if the price is unattractive, the argument that a good name assures a good shaver. The purchaser can learn little as to the true worth of a product from either line of talk.

"The price appeal can be especially misleading. Electric shavers are being offered the public today at prices ranging from 98 cents to $50. There is no valid reason for such wide difference in prices. Even among the medium group of shavers with the best consumer acceptance, there is a price spread of $7.50. The one valid reason for a difference in price among shavers is that one of the three types of motors used may cost about $2 more to produce than another.

"An instrument of such complexity as an electric shaver usually cannot be well made and sell at less than $5. When sold for less today, it is likely to be inferior in materials, workmanship or design. The more expensive 'luxury' models add only a gold plating, more attractive case or a fancy box, none of which materially improve their performance.

"Wise buyers will pay very little attention to price appeal, whether the bait is a low or a high price.

"Nor is the fact that an old or big company is behind a particular shaver necessarily a sign that the shaver is better than any other. It is well, however, to be sure that the company is sufficiently well

[1] Woodward, Helen, *Through Many Windows*, p. 309, Harper & Brothers, New York, 1926.

established to make good on its claims and to furnish parts and make repairs when they become necessary."[1]

From a producer's point of view there may be much in a name. Modern accounting practice recognizes the cash value of good will. From a consumer point of view, however, a name may mean little or nothing. It is essential that consumers interested in promoting their own welfare develop some means for getting behind trade names and ascertaining the true relation between quality and price.

Summary

The main argument of this chapter is that price is not a reliable guide to quality of merchandise. If the assumptions of value theory were valid, consumers could depend on price as a measure of quality, but competition does not operate to maintain one price for identical merchandise in a given market, consumers are unable to judge quality, and they vary considerably in bargaining ability. In their ignorance they rely on price as a guide to quality, and sellers seek to benefit by boosting their markups. Contrary to the law of demand, many consumers are positively attracted by high prices. Nominally the United States is a one-price country, but actually the bargaining system is in wide use. This confusion of practice operates to the disadvantage of all consumers, except a very few who are or try to be economic men.

QUESTIONS FOR DISCUSSION

1. When you pay ten cents to ride on a bus does that price accurately measure the value to you of a ride? Would your conclusion differ if you were paying ten cents for a ride on a merry-go-round?
2. Prior to reading this chapter had you thought of the United States as a country where buyers and sellers deal on a bargaining basis or on a one-price basis? Have you ever bargained when making a purchase? Do you have any objection to bargaining?
3. Does the one in your family who does most of the buying of provisions, appliances, furnishings, furniture, and clothing shop around?
4. Before reading this chapter did you believe that "you get just about what you pay for"? Do you still think so?
5. What is the "law" of one price? Is it valid?
6. Were you previously aware of the extent of retail markups? Can you add additional illustrations?
7. In view of prevailing high markups why are not all retailers wealthy?
8. To what extent have you and members of your family followed price as a measure of quality?

[1] Household Finance Corporation, *Better Buymanship*, Bulletin No. 27, p. 10, Chicago, 1940.

9. Compare the brand of gasoline used to fuel the family car with brands used by the families of others in the class; how much do you really know about the relative qualities of the several brands? How much more (or less) do you think those who buy the gasoline know?
10. How often has the oil been changed in your family car? Why?
11. How well qualified are you to test the quality, before buying, of sheets, shoes, silk stockings, rugs, fur coats, cosmetics?

PROBLEMS AND PROJECTS

1. Secure and compare prices for identical goods in a given market at the same time. Does your evidence support the law of one price? Note: This project will be more effective if several students co-operate.

2. Assume that you are buyer for a family of five. Draw up a list of your needs for one week, then shop at four or five stores and compare prices. In your report show how much you could save by purchasing for the lowest prices.

3. Fortify yourself with Consumers' Research or Consumers Union information concerning gasoline and oil; then ask attendants at five filling stations for information concerning their particular products. See if you can secure enough facts to make an intelligent purchase.

4. Take several products not included on pages 239, 240, and discover, if you can, what it costs to make them; then compare those figures with retail selling prices.

5. Assume that you are going to buy an automobile, a mechanical refrigerator, or a washing machine. Compare at least four different machines, securing prices and as much information as you can from salesmen. See if you can secure a concession in price. After deciding, on the basis of salesmen's information, which machine you would buy, compare your conclusions with those of Consumers' Research or Consumers Union.

14

Making It Easy to Buy: Installment Selling

Cash or Credit?

What Is Buying? Buying and its necessary counterpart, selling, are characteristics of modern exchange economy. In a primitive economic system characterized by a high degree of self-sufficiency there is a minimum of buying and selling. As specialization develops it becomes necessary to exchange one's goods or services for those produced by other specialists. Buying may be defined as acquiring goods or services by giving a price for them. In our modern economic system it is a necessary step for the satisfaction of consumers' wants. The process of exchanging goods or services for goods or services is accomplished in the market through the medium of money or credit. It is the latter which has grown apace in retail transactions and with which this chapter deals.

Buying implies the exchange of goods and services for cash in possession of the buyer. But a buyer may give a promise to pay in lieu of cash. This may be an unsecured promise which does not create a net debt,[1] or it may be an unsecured or secured promise to pay out of future income, thus creating a debt. The long-established practice of purchasing goods on open account illustrates the first type of credit, while the more modern method of purchasing on the installment plan is typical of the second. In both of these cases the buyer is securing from the merchant not only the merchandise which he wants but also the credit which he needs. The merchant in turn may secure from a banker or finance company the necessary capital to carry these accounts.

If the merchant is not able or willing to combine the sale of credit with the sale of his merchandise he may insist that his customers pay him in cash. This does not, however, prevent the buyer from securing goods or services on credit. It simply means that he must secure his credit else-

[1] If one has $1,000 invested in stocks or bonds those could be sold to get cash with which to purchase a new automobile. But if, for various reasons, one does not wish to sell the securities, one may borrow $1,000. Such a loan, being offset by equivalent assets, does not create a net debt; a loan of $1,500 would create a net debt of $500.

where. He may, for example, negotiate a loan at a bank, using the proceeds to buy the things he wants. This is a common practice among businessmen but less common among consumers. Bankers regard loans to businessmen as productive, that is, self-liquidating. Loans to consumers are regarded as nonproductive, with the result that banks are much more hesitant in granting credit to consumer borrowers.

Persons who hold life insurance contracts have a source of credit which is commonly used, as will be explained in the chapter on insurance. These policyholders may borrow a portion of their accumulated reserve, using the policy itself as security for the loan. Insurance reserves represent savings, so consumers who resort to this means for securing cash are really using their own savings rather than their credit.

A similar situation exists in the case of loans secured by real and personal property. If a consumer owns real property or shares of stock or bonds such wealth may be converted partly and temporarily into cash by means of a mortgage.

Another source of credit used by money borrowers whose incomes are limited is the small-loan agency. Operating primarily to provide credit for needy consumers, these agencies differ from commercial banks primarily in the types of loans granted and the rates of interest which they charge.

Comparative Volume of Cash and Credit Buying. In any of these cases the consumer borrower is securing present goods or services on the basis of his promise to pay for them in the future. The total amount of credit involved is large because the number of consumers is large. Although not usually regarded as business enterprises, the millions of individual households constitute one of the largest and most important of economic enterprises. Approximately 33,000,000 women are employed in managing these households, which represent an estimated investment of $158,000,000,000. In 1942 purchases by these 33,000,000 buyers accounted for a large portion of the $56,000,000,000 worth of goods sold at retail. About 27 per cent, or $15,100,000,000 worth of retail sales were made on a credit basis. Of that amount approximately $12,300,000,000 represented open charge accounts, while $2,800,000,000 represented installment sales. The latter figure, of course, was much smaller in 1942 than in 1940 and 1941, as a result of the Federal war policy of restricting consumer credit. In 1941, for example, $19,300,000,000 worth of merchandise was sold on a credit basis; of that amount $6,800,000,000 represented installment sales.[1] The foregoing figures refer only to retail

[1] Board of Governors of the Federal Reserve System, *Retail Credit Survey, 1942*, p. 1, Washington, 1943. The effect of war on consumer credit is considered in Chapter 29.

sales of merchandise. If all credit sales of services as well as of goods are included, the volume of consumer credit outstanding is much larger. In the middle of 1941 it was estimated to be $8,800,000,000, the highest on record, topping the 1929 peak by $700,000,000.[1]

Obviously the use of credit makes it easier to buy. Extension of retail credit has become a popular modern means of temporarily expanding the market for consumers' goods and services. Consumers as a group represent a bundle of wants. They have many more desires than they are able to satisfy. Profit-seeking producers have found in this situation an opportunity to induce potential consumers to buy on credit when they could not buy for cash. This new development in retail merchandising, which dates from the period following the war of 1861–1865 but has achieved its present significance only since World War I, constitutes a new force affecting consumer demand. No longer is it necessary for a buyer to have cash in hand to make a purchase. Faced with an intense desire to enjoy some of the comforts and luxuries forced on his attention by advertising and salesmanship, his last ounce of resistance is broken down by the assurance that he can have whatever he wants by paying only a few cents a day.

Why Buy on Credit?

Reasons for Buying on Credit. It might be supposed that the very fact of a credit purchase is evidence of the buyer's inability to pay cash. This is not necessarily the case, however. Probably many credit transactions are incurred for the sake of convenience. This is particularly true of open-account buying, which is the oldest form of credit and the largest in volume. By a great many users this form of credit is employed not so much because of inability to pay cash as for the convenience in keeping a record of accounts and making payments out of income earned currently or in the past. The traditional form of open-account credit with retail merchants grants the buyer a week to a month in which to pay his account. This is based on the customary method of paying wages and salaries, the expectation being that buyers will settle their accounts upon receipt of their pay checks. In many cases customers who are quite able to pay cash either out of current income or out of savings find it convenient to make payments in periodical lump sums.

For a great many buyers, on the other hand, open-account credit represents actual net debt. In such cases the merchant is permitting them to acquire goods and services on the promise of deferred payment without making an extra charge.

In either case the retail merchant who permits customers to purchase

[1] *New York Times*, July 17, 1941.

on open account is selling a service in addition to merchandise. The service is that of supplying credit, traditionally a function of commercial banks and one for which buyers must pay either in the form of a specific price or in the form of higher prices for the merchandise. Actually the burden is often divided, cash buyers bearing a part of the cost in the form of prices higher than they would have to pay at a store selling only on a cash basis. The balance is carried by customers who use the credit facilities. Several years ago the New York State Food Commission made a study of credit costs. It was estimated that consumers trading in well-to-do neighborhoods paid an average of $22.36 a year each for delivery and credit. In those neighborhoods in which buyers of limited incomes predominated, only 10 per cent made use of delivery service and only 20 per cent expected open-account credit. Another investigation revealed that the retail price of sixteen staple goods sold by cash-and-carry stores averaged 17.33 per cent less than prices charged by stores providing delivery and credit service.[1]

The additional expense of carrying charge accounts over and above cash accounts in a St. Louis retail store amounted to 5.34 per cent of sales. This is broken down into ten items covering collection expenses, postage, salaries, credit reports, office supplies, depreciation on equipment, losses on bad debts, and interest on outstanding accounts.[2]

The cost of granting credit in various types of retail businesses expressed as an annual rate was 20 per cent for general grocery stores, 18.6 per cent for automobile repair shops, 17.4 for hardware stores, 16.3 for gas and oil stations, and 10 per cent for new automobiles.[3] Borrowers are accustomed to paying six per cent for the use of funds. But they are accustomed to paying that only at banks, not at retail stores. Nor are they usually willing knowingly to pay more than that rate. Of course, those who extend credit must in the long run charge what it actually costs them, so devious devices are used to make it appear that there is either no charge or that the charge is no more than six per cent.

Open accounts are based almost entirely on personal credit. Seldom, if ever, is the buyer asked for any tangible evidence of indebtedness or to give any form of security. As the system operates, a person who, either from necessity or from choice, pays cash at a store allowing open accounts, is at a distinct disadvantage not only in higher prices paid, but in fewer services rendered. If, for example, a purchase proves unsatisfactory, an open-account buyer enjoys a distinct advantage over the cash buyer

[1] Harap, Henry, *The Education of the Consumer*, p. 56.

[2] Phelps, Clyde William, *The Ten Hidden Losses in Charge Accounts*, p. 7, Household Finance Corporation, Chicago, 1937.

[3] Maughan, Orlo, "The Cost of Store Credit," p. 20 in *Cornell Extension Bulletin*, New York State College of Agriculture, Cornell University, Ithaca, New York, April, 1936.

in securing adjustment. At the same time this practice invites abuse by unscrupulous buyers who seek to return merchandise after using it.[1]

A second reason why buyers resort to credit is to meet emergency situations. This is particularly true in lower-income groups. A study of 10,000 small loans showed that 75 per cent of the borrowers earned less than $40 a week, with 33 per cent earning less than $30 a week. Another study of 24,000 small loans indicated that 33 per cent were incurred to meet current family expenses, 33 per cent to liquidate other debts, 10 per cent to cover expenses incident to illness or death, and 10 per cent for business purposes.[2] In many cases it was difficult to ascertain the real reason for the loan. An emergency may have depleted family resources, yet the purpose of the loan would be given as that of meeting current family expenses. Illness, accident, and death require unexpected expenditures, while unemployment eliminates anticipated income. Families with little or no reserve have no choice between the use of cash and of credit. Their first tendency is to turn to merchants and professional men in expectation of receiving merchandise or services on open account; but it is understood that when the emergency has passed the account will be paid. Sometimes, but not usually, an interest charge is added. In these cases merchants and professional men combine the functions of banker with those of their own business or profession.

However, if the account grows large, creditors may, for the sake of legal protection, require negotiation of notes with interest and provision for regular payments on the principal. Many merchants, however, do not possess the necessary capital or managing ability to perform these essentially banking functions, as is evidenced by the large number of business failures accredited to overextension of credit.

For some reason prospective borrowers have much less hesitancy in asking a merchant to carry their accounts than they have in asking a banker to lend them the necessary credit to enable them to pay cash for all merchandise purchases. On the other hand, merchants seem to find it much more difficult than bankers to refuse a request for credit. Actually, provision of credit is essentially a banking function and one which in this day of specialization should be limited to banks and recognized lending institutions. Traditionally, however, bankers have regarded themselves primarily as providers of credit for businessmen. As a result they have turned the field of consumers' loans over to loan brokers, small-loan companies, and Morris Plan banks. When consumers are faced with an emergency and no longer are able to secure open-account credit they are

[1] Peffer, Helen, and Newton, Juna, "They Want Their Money Back," in *Atlantic Monthly*, vol. 148, p. 181.

[2] Clark, Evans, *Financing the Consumer*, pp. 179, 180, Harper & Brothers, New York, 1930.

forced to turn to one of these small-loan agencies. Since their action is not usually a matter of choice but of necessity, the operation of institutions granting consumer loans has been subject to wide abuse. Variation in loan charges is shown in the following table.

TABLE XX.—BORROWERS' GUIDE TO ACTUAL COST RATE OF SMALL LOANS[1]

Loan Agency	*Common Charge (Per Cent)*	*Range of Charges (Per Cent)*
Savings Bank Accounts	—	3–6
Building and Loan Association Shares	6	6–12
Insurance Policies	5	3–6
Credit Unions	12	6–18
Personal Loan Departments of Banks	12	7–23
Remedial Loan Associations (Pledges)	—	9–36
Remedial Loan Associations (Chattel Mortgages and Co-maker Notes)	—	15–30
Industrial Banks	17	12–34
Pawnshops	36	24–120
Personal Finance Companies	36	30–42
Installment Sellers and Finance Companies	—	0–500
Illegal Lenders	240	72–1200

Impatience of consumers is a third reason for the extensive and increasing use of credit. People live in the present and value present goods and services much more highly than the possibility of greater satisfactions in the future. The future is altogether uncertain. This uncertainty reacts on a few people in such a way as to compel them to take every possible precaution to provide for their future well-being. For most people, however, the reaction is quite different. They are much more concerned with present well-being and security, usually content to let the future take care of itself if and when it comes. From the standpoint of consumers this is probably more true today than formerly. One reason is that goods are now produced almost entirely in anticipation of consumers' demand. This means that with much less strain on their imagination buyers can visualize present satisfactions while future satisfactions seem more remote.

Producers, in their efforts to secure economies of large-scale production, attempt to expand their individual markets by advertising and salesmanship. Encountering limited purchasing power, they are forced to make it easier for consumers to buy. The net result has been the phenomenal growth in the volume of installment selling.

Because of their preference for the present over the future, people find it difficult to save. If this were not the case there would be no reason

[1] Foster, LeBaron R., *Credit for Consumers*, p. 21. The Public Affairs Committee, New York, 1939.

why buyers could not save enough money in advance to pay cash for their purchases. As it is, consumer buyers cannot visualize the enjoyment they will receive from a radio twelve or eighteen months from now, but if they possess the radio and enjoy its use in the present they find it easier to save and pay in the future, even though this method requires the outlay of many more dollars. It is not surprising to find that nearly 25 per cent of the non-relief families in the United States made use of installment credit in 1935–1936, and that the extent of its use varied with the income level. The proportion of families in each income class indebted for installment purchases rose steadily until the income bracket \$1750–\$2000 was reached, after which it declined consistently. It is interesting to find that installment credit is used much more by city consumers than by rural consumers. In 1935–1936 approximately 70 per cent of installment purchases were made by city people. For all income classes installment purchases were larger in the large, small, and medium-size cities. Moreover the use of installment credit seems to vary among regions, according to the 1935–1936 study. In the Pacific Region one third of all farmers were installment debtors; one fifth in the North Central Region; and one fourth in all other regions.[1]

Two additional reasons may be mentioned together. Experience has shown that many people who could pay cash prefer to buy on credit because they fear that they might not replace their savings, once they were spent. Others make use of credit because it requires a budgeting of income and encourages them to spend for more durable goods.

Impatience Leads to Installment Buying

Nature and Development of Installment Buying. In a broad sense, the purchase of merchandise on the installment plan of payment is an ancient practice. Crassus, a contemporary of Julius Caesar, sold Roman houses on this plan. Every feature of installment selling is old, but the various parts of the modern system were never joined before the middle of the nineteenth century. Seligman credited Cowpersthwait and Sons of New York with inaugurating a plan for selling furniture on the installment basis as early as 1807. From furniture the plan spread to household articles in general. Singer sewing machines were first offered for sale on the installment plan about 1850; and pianos in 1875. In that same period the sale of books on the installment plan also was inaugurated.[2]

[1] Bernstein, Blanche, *The Statistical Pattern of Instalment Debt*, pp. 3, 8, National Bureau of Economic Research, New York, 1939.

[2] Seligman, E. R. A., *The Economics of Instalment Selling*, vol. 1, chaps. 1–5, Harper & Brothers, New York, 1927. Isaacs, Nathan, "Instalment Selling: The Relation Between Its Development in Modern Business and the Law," in the Duke University Law School's journal, *Law and Contemporary Problems*, vol. II, April, 1935, pp. 141–147.

The sale of houses on the installment plan through building and loan associations has long been accepted as good merchandising practice. But the sale of what are known distinctly as consumers' goods on the installment plan is comparatively recent in origin. A rapid growth of population and development of a large-scale, impersonal market provided the modern need for a new merchandising method. A secondhand market is essential to installment selling. This development may be said to date from the post-World War I period. Formerly there was a strong prejudice against installment selling. Respectable people refused to use that means of buying. Today the situation has changed, and installment buying has become respectable.

Most of these changes have resulted from the tremendous development of installment selling of automobiles. This method of merchandising a new high-priced commodity began about 1916. Automobile manufacturers, eager to stabilize production and increase sales, were forced to invade the potential market represented by millions of low-income consumers. Supplemented by the finance company, installment selling spread rapidly in the early 1920's, following its success in merchandising automobiles. The greatest development occurred in the case of new products or old recognized articles whose producers had not previously used this new selling method. Phonographs, radios, washing machines, vacuum cleaners, mechanical refrigerators, gas stoves, jewelry, and clothing have been sold to many consumers on the installment plan. By 1926 the total volume of installment sales exceeded $5,000,000,000 a year. During the next five years installment sales amounted to over $5,000,000,000 annually. They dropped to approximately $4,000,000,000 in the early 1930's, but rose to a new height of $6,500,000,000 in 1937.[1] By 1940 rail passenger transportation could be purchased on the installment plan. Travelers Credit Corporation arranged with approximately 2,500 banks throughout the country for acceptance of notes signed by individuals who desired to secure railroad transportation on the installment plan. Amounts borrowed were repayable in twelve monthly installments at an interest rate of 8 per cent on the total amount of the note. During the two-year period in which the plan was in operation prior to its discontinuance because of World War II, 66 of the leading railroads participated in the plan.[2]

Economic Aspects of Installment Buying. Seligman defined installment sale or purchase as "a transfer of wealth, the payment for which is deferred in whole or in part to the future and is liquidated piecemeal or in

[1] *Business Week*, November 25, 1939.

[2] *New York Times*, May 8, 1940; and correspondence with Trans-Continental Passenger Association.

successive fractions, under a plan agreed upon at the time of transfer."[1] Plummer describes an installment sale or purchase as "one in which the price of the goods is to be paid in fixed portions at stated intervals."[2] It will be seen that the essential characteristic of an installment sale or purchase is repayment in fractional amounts over a stated period of time. Usually, though not necessarily, title to the wealth transferred remains with the seller. In case of default all payments are usually forfeited and the merchandise repossessed.

Probably the outstanding economic function of this new form of credit is its ability to provide consumers with high-priced merchandise in the present, using that merchandise as security for full payment. This means of course that the buyer is paying not only for the merchandise, but also for the credit. As a matter of fact, the buyer pays for a number of other services usually performed by the finance companies, such as "the cost of checking the applicant's credit position; insurance, if required; setting up of service machinery for the handling of the collection of the account; the cost of the money advanced immediately to the dealer; a credit reserve; and a reasonable profit."[3]

When these finance charges are added to the cash price of merchandise its cost to the ultimate consumer is definitely increased. The amount of that increase will vary with commodities and among finance companies. In 1927, when the first great wave of installment selling was at its height, Plummer found the cost of installment credit on general merchandise such as furniture, radios, and household equipment ranging from 11 to 40 per cent. In one case the rate figured 84.5 per cent. Rates on new automobiles varied from 11 to 23 per cent, while the rates on used cars ranged from 16 to 43 per cent. In neither case were insurance costs included.[4]

In the same year Seligman made his study of installment selling, discovering practically the same costs being levied on consumers. He worked out a system of coefficients for determining the actual finance charges, which showed a rate of 26.7 per cent on new cars and 38 per cent on used cars. A sewing machine company was using a series of rates which figured up to 48 per cent.[5]

During the following decade finance companies would have consumers believe that costs of installment buying have been reduced. Until

[1] SELIGMAN, E. R. A., *The Economics of Instalment Selling*, vol. 1, p. 2, Harper & Brothers, New York.

[2] PLUMMER, W. C., "Social and Economic Consequences of Buying on the Instalment Plan," in *The Annals*, 1927. Supplement to vol. CXXIX, p. 1.

[3] Commercial Investment Trust (of New York), *Buying out of Income*, p. 12. This corporation is a finance company, first organized in 1908.

[4] PLUMMER, *op. cit.*, p. 30.

[5] SELIGMAN, *op. cit.*, pp. 289–290.

the Federal Trade Commission ordered them to cease, the major automobile companies had been featuring the so-called 6 per cent plan in their advertising.[1] This was presented in the following way by the Commercial Investment Trust:

Suppose the cash delivered price of the car you intend to buy is	$850.00
Now subtract whatever cash down payment you make plus the trade-in allowance on your old car. For example	290.00
Therefore, your unpaid balance is	$560.00
Then add the insurance premium (including a nominal documentary fee, if required). Assume this is .	40.00
This gives you a total of	$600.00
C.I.T. financing charge (in this case for 12 months) upon this total is.	$36.00
Adding the financing charge to the total arrived at above, namely	600.00
Gives you the total amount of your contract. . . .	$636.00
Divide this figure by the number of months required (in this case 12) to determine the monthly payment	53.00

Your car is insured for its actual value against loss by fire and theft, and accidental physical damage, including collision (deductible), tornado, flood, hail, cyclone, falling aircraft, windstorm, riot, explosion, and earthquake.

This is in fact a 6 per cent *plan*, but is not a 6 per cent *charge*. No provision is made for reducing interest payments as the principal is reduced $50.00 a month. By this method, the actual cost of the installment credit to the consumer figures 11 to 12 per cent.

Froman converted the finance charges of several installment merchants and finance companies into annual rates based on unpaid balances. For new automobiles rates varied from 14 to 38 per cent; for electric appliances, 13 to 23 per cent; for electric refrigerators, 14 to 30 per cent; for miscellaneous merchandise distributed by a mail-order house, 13 to 66 per cent.[2]

A similar study covering 60 stores in a Middle Western state made by Foster in 1934 yielded the following results:[3]

[1] Federal Trade Commission, *Decisions*, vol. 31, pp. 1852–1858; vol. 33, pp. 1781–1795.

[2] Froman, Lewis A., "Cost of Instalment Buying," in *Harvard Business Review*, January, 1933, quoted by Nugent and Henderson in *The Annals*, May, 1934, p. 98.

[3] Foster, William Trufant, and Foster, LeBaron R., "Rate Aspects of Instalment Legislation," in the Duke University Law School's journal *Law and Contemporary Problems*, vol. II, April, 1935, p. 190.

TABLE XXI.—INSTALLMENT PURCHASE COST RATES FOR SELECTED MERCHANDISE IN 60 STORES IN 1934

Commodity	*Per Annum Cost Rate (in Per Cent)*
New automobiles *	21.9 to 32.9
Used automobiles *	34.8 to 47.1
Refrigerators	8.3 to 51.8
Furniture	6.0 to 55.5
Radios	11.5 to 98.3
Automobile tires	33.6 to 106.1
Stoves	0 to 68.6
Other commodities	0 to 103.7

* Includes fire, theft, and sometimes collision insurance.

All these figures, together with those disclosed in 1936 by the Massachusetts Committee on Consumer Credit and the Special Commission appointed by the Massachusetts General Court, go to prove that installment credit costs have not diminished in recent years. The lowest rate charged in the case of a new car purchase was 10 per cent, while the highest rate was 36 per cent. For used cars the rates were still higher, while the rate on an auto radio figured to 943 per cent.

Table XXII, on page 272, shows the lowest and highest installment credit charges on 23 commodities and services.

Are installment credit costs too high? Disregarding extreme cases, spokesmen for finance companies contend that the method of showing costs as an annual interest rate is objectionable because it assumes that the finance charge represents a pure interest rate for the use of credit. Actually, as has been shown, charges for a number of services are included. Yet from the buyer's point of view it makes no difference whether credit costs are considered as interest charges or as interest charges plus service costs. The net result is that the credit price is considerably more than the cash price. Whether or not this differential is too great is a difficult question to decide. It may be contended that if a buyer needs or wants his goods badly his willingness to pay a considerable differential is in itself evidence that the price is fair, for otherwise the installment purchases would not be made. This assumes, however, that the buyer is fully aware of the costs involved. As a matter of fact, installment credit costs are so concealed by a variety of methods that the average buyer is unaware of their extent. Few buyers possess the knowledge of mathematics necessary to make an accurate comparison of cash and installment prices.

A simple, convenient method for making a rough comparison is that which makes use of an annual cost rate.

"The cost rate, as in the case of an interest rate, may be found by dividing the credit charge by the average amount of credit extended for one year; for example, if a purchaser paid $6.50 for the privilege of financing a $120 balance over a twelve months' period, he would receive, on the average, $65 for a full year ($120 the first month, $110 the second, $100 the third month, and so on, down to $10 in the last month, averaging $65 for the whole period), and $6.50 divided by $65 would give the cost rate of 10 per cent."[1]

TABLE XXII.—COMPARISON OF ACTUAL COST RATES FOR INSTALLMENT CREDIT IN MASSACHUSETTS CITIES IN 1935[2]

Commodity	*Lowest Rate* Rate Quoted by Seller	Actual Rate	No. of Payments	*Highest Rate* Rate Quoted by Seller	Actual Rate	No. of Payments
	per cent	*per cent*		*per cent*	*per cent*	
New automobiles	—	10	18 monthly	—	36	12 monthly
Used automobiles	—	0	25 weekly	—	457	5 monthly
Refrigerators	5–6	9	12 monthly	5	58	12 monthly
Radios and phonographs	0	0	21 monthly	—	881	13 weekly
Pianos	6	6	24 monthly	—	184	65 weekly
Musical instruments	0	0	8 monthly	—	44	10 monthly
Furniture and rugs	0	0	12 monthly	—	330	13 weekly
Washing machines	6	9	24 monthly	6	114	6 monthly
Vacuum cleaners	5	8	6 monthly	—	47	6 monthly
Sewing machines	5	9	16 monthly	—	73	10 monthly
Stoves, ranges, and range burners	0	0	44 weekly	—	404	3 fortnightly
Oil burners and heating equipment	4	8	36 monthly	—	325	7 weekly
Jewelry	0	0	72 weekly	0	618	3 monthly
Men's clothing	0	0	28 weekly	0	0	7 weekly
Women's clothing	0	0	9 monthly	—	117	9 weekly
Auto radios, equipment, and repairs	0	0	4 weekly	—	943	16 weekly
Tires	0	0	12 weekly	—	800	1 monthly
Motorcycles	—	29	12 monthly	5	42	12 monthly
Bicycles	—	59	15 weekly	6	679	3 weekly
Typewriters	0	0	23 weekly	6	80	5 monthly
Coal	—	37	5 monthly	—	532	4 weekly
Dental services	—	405	10 weekly	—	405	10 weekly
Group purchases	—	22	20 weekly	—	55	20 weekly

[1] Committee on Consumer Credit, Commonwealth of Massachusetts, *Report*, pp. 47, 48. See also a helpful pamphlet entitled *One Hundred Problems in Consumer Credit*, available for 10 cents at the Pollak Foundation for Economic Research, Jaffrey, N. H. Also *Consumer Credit Cost Calculator*, available from Household Finance Corporation, Chicago.

[2] Massachusetts General Court, Special Commission, *Report*, quoted in Committee on Consumer Credit, Commonwealth of Massachusetts, *Report*, February 17, 1936. See text on page 271.

A still more simple method is that of doubling the apparent or quoted rate. This can be used, however, only when the quoted terms are based on a twelve months' period and even then is only a rough approximation. Either of these methods will serve to help a prospective buyer discover what the privilege of installment buying is going to cost.

Whether or not installment credit costs are too high cannot be determined on an absolute basis. Account must be taken of the advantages claimed for this method of buying.

Advantages of Installment Buying. Probably the outstanding service of installment credit is the breaking up of total payments into fractional payments. By this means persons receiving small incomes find it possible to purchase high-priced durable goods. Moreover, buyers are permitted to enjoy the use of these goods while paying for them. Alternatives to this method of purchasing are to save first and pay cash at the time of purchase or to save while using the commodity and pay the full purchase price in a lump sum. It may be contended that use of the first alternative is much wiser since the buyer not only does not pay any interest or finance charges, but actually receives interest on savings accumulated for the purchase. This assumes that the buyers are sufficiently patient to forgo immediate enjoyment of things they want for a comparatively long time. It has already been shown that the rate of impatience is a subjective factor which varies among individuals. Some consumers are willing and able to wait for enjoyment of economic goods until they can purchase for cash. Others are neither willing nor able to accumulate a cash reserve in advance. In between is a third general group of potential buyers who would be willing to wait a reasonably long time, but whose incomes are so small that enjoyment of certain goods would have to be postponed too long a time awaiting their accumulation of the purchase price. It is obvious that they cannot save any faster while using the commodity than while anticipating its acquisition. In fact they cannot save the full purchase price as quickly, because they pay interest instead of receiving it. But many people find the incentive to save less strong than the necessity of meeting an installment payment.

It has already been shown that the method of installment buying has long been applied to the purchase of homes. Few indeed are the number of persons who would be able to pay the full purchase price of a house at the time of purchase. Until automobiles were offered for sale on the installment plan the number of buyers was relatively small. Widening the field of consumer credit so as to include such recently developed commodities as radios, washing machines, vacuum cleaners, mechanical refrigerators, and many other modern household appliances is regarded as nothing more than a logical development of a merchandising method

which has proved its worth. Seligman pointed out that as a matter of practice down payments which range from 25 to 40 per cent of the total purchase price are equal to or in excess of the present enjoyment received by the buyer. This means that the purchaser may be regarded as paying a rental for the use of a commodity, the rental being applied to the purchase price so that ultimately he becomes the full owner. Whether or not the satisfaction of present use is worth the price required depends upon the charge made for the privilege of installment buying. Figures revealing these charges have been given. No objective application can be made, for a charge which may seem too high to one buyer will be acceptable to another, depending upon individual subjective satisfactions. What the average buyer on the installment plan sees and understands is that by deducting a few dollars per week or month from his income he will be able to acquire at once the article which he so keenly desires. In all probability not one out of ten makes any effort to calculate the comparative cash and credit prices. For their cases, there is no alternative. If previous commitments will permit including an additional purchase it will no doubt be made even though finance charges may run to 50 per cent or more.

A second advantage claimed for installment credit is that it compels the habit of saving. Persons who would otherwise fritter away their incomes are disciplined by incurring obligations which must be met regularly. It is not likely that buyers responsible for the several billion dollars worth of annual installment purchases would save enough in advance voluntarily to enable them to pay cash for their purchases. Amounts going to installment collectors would in all probability be used for temporary satisfactions. Account must be taken also of the fact that in many localities such as mining camps and rural regions facilities for saving are few and scattered. Experience has shown also that they are none too secure. It is not surprising that a coal miner will save much more readily if he is making weekly payments on an automobile or radio than if he is attempting to build up an account in a bank whose operation he does not understand and of whose security he cannot be certain. Persons in the middle-income group do most of their saving by purchasing life insurance. But that method of saving is practically closed to lower-income groups. Their incomes will not permit the purchase of regular insurance; in fact in some cases they cannot purchase any insurance because of occupational hazards. The only type of protection available to those people is the industrial insurance policy, the rates of which are so high that it is an open question whether an unskilled worker is any wiser in trying thus to save and provide for the future than his friend and neighbor who decides to enjoy life in the present by purchasing a

commodity which will yield immediate satisfaction. The annual premium quoted by a standard company on a $1,000 nonparticipating life insurance policy at age 20 is $14.63, while the rate on an industrial policy figures out to $60.00.

Much that has been said in the preceding paragraph supports the contention that a third advantage of installment buying is its possible encouragement of a wiser use of income. To the extent that this is true, it would apply primarily to persons of the lower-income group, among whom installment purchases are largest. The tendency of such people to discount the future has been sufficiently emphasized to justify the conclusion that if they did not have the incentive to save provided by the installment plan of purchase they probably would not save amounts equal to their installment payments. Amounts paid in weekly or monthly installments which now result in acquisition of durable goods might be spent on goods or services capable of satisfying only passing desires.

What has been said in this section may be summarized by saying that if all consumers were wise, that is, well-educated and good buyers, the installment purchase device would be less widely used. Taking consumers as they are, however, and giving due regard to their limited incomes, this modern method of merchandising may serve to encourage saving and the purchase of more useful, durable commodities. But this conclusion should not be accepted without examining some of the more common abuses associated with installment selling.

Abuses of Installment Credit. Installment selling is the handmaiden of modern advertising and high-pressure salesmanship. It is a commonplace of economics that human wants are unlimited. As the modern economic machine has devised and perfected innumerable new commodities, the task of selling them has been not so much that of creating desire as of contriving a method to enable purchase. That method has been found in the installment credit plan. Until comparatively recent times the last defense of consumers against the onslaught of high-pressure methods of selling has been inability to meet the purchase price. Installment selling has broken this last barrier, making it still easier for modern salesmen to dispose of their wares. That this is not an altogether undesirable development has already been suggested. But when advertising is fortified by installment credit to force the sale of nealth or illth it becomes an instrument for promoting illfare rather than welfare. It is common practice among installment merchants selling cheap jewelry, clothing, and furniture to put up their prices, spending part of the extra margin on high-pressure salesmanship and legal fees.[1]

[1] NUGENT, Rolf, and HENDERSON, Leon, "Instalment Selling and the Consumer: A Brief for Regulation," in *The Annals*, May, 1934, p. 96.

The National Credit Association adopted a resolution describing the tendency toward liberalizing credit, particularly the advertising of such terms, as "extremely dangerous." The use of such terms as "no down payment" and "pay as you please" is condemned, as is "high-pressure salesmanship to load people up with a lot of things they do not need." The resolution concludes that "it is recognized that such practices lead to continued unprofitable competition resulting in no advantage to the retailer and a decided disadvantage to the consumer."[1]

A number of fraudulent practices have grown up which are peculiarly associated with installment selling. In conjunction with advertising is powerful persuasion on the part of salesmen concerning commodities that are commonly misrepresented to buyers who are incapable of judging their quality. A certain workman was induced to buy a watch for $40 on the representation that it was real gold with seventeen jewel movements and would last a lifetime. The selling point was that the buyer need pay only $2.00 down and "a little each week." Appraisal of the watch by a competent jeweler resulted in a valuation of $19.75. A Portuguese workman was induced to buy a diamond ring on approval at the rate of $3.00 a week. He was asked to sign a receipt which later proved to be an agreement of purchase at a price of $100 for a cheap chip diamond valued at $25.00.[2]

A common practice in the sale of furniture on the installment plan is delivery of a cheaper grade than that displayed at the time of sale. In connection with automobile purchases buyers have had their cars repossessed only to find it necessary to pay repossession costs amounting to as much as $65 in order to recover their property. In fact, automobile sales and financing abuses were so widespread by 1940 that the Columbus Better Business Bureau issued a special bulletin on the subject and the Committee on Automobile Financing Abuses of the American Automobile Association included in its report this statement: "... It is the definite conclusion of your Committee that evils amounting to scandal exist in the financing of automobiles and automobile accessories, and that abuses are wide-spread, flagrant and of long standing."[3]

A third common abuse associated with installment selling concerns the powerful legal instruments which are used by the seller. Technicalities of the law and the courts are all on the seller's side. A conditional sale agreement is so complicated that few if any buyers read or understand it. Indeed it would do them little good if they did. For a great many buyers who are able to meet their payments regularly no diffi-

[1] *New York Times*, June 19, 1936.
[2] Nugent and Henderson, *op. cit.*, pp. 94–95.
[3] Columbus Better Business Bureau, *Bulletin*, July 9, 1940, p. 1.

culties arise. But in the case of others whose anticipated income is less than was expected, the power of the legal instruments covering the sale is quickly revealed. Even though all but one payment may have been made, the merchandise may be repossessed, causing the buyer to forfeit all payments made. There is no escape from a purchase which has proved unsatisfactory, for at the time of sale the unwary buyer may have given the seller a power of attorney. This instrument may be used to secure the assignment of all wages due an employee until the amount is paid. Moreover, wage assignments are valid against all subsequent employers. In one year eight New York employers of 105,000 men reported 1,900 powers of attorney to collect wages for installment merchants, over half of whom operated jewelry and clothing stores. Other studies revealed a high percentage of wage assignments, in one company as many as 50 per cent of the employees being involved.[1]

Ignorance of the average consumer concerning the ways of the market and wiles of the seller is exceeded only by his ignorance and fear of the law. The vast majority of substantial citizens are law-abiding and law-respecting. When through their ignorance they find themselves in the toils of the law they are likely to become panic-stricken and easy prey for unprincipled representatives of cheap installment firms. There can be no doubt that a great many installment buyers permit themselves to be victimized by legal chicanery rather than suffer the embarrassment and humiliation of reporting their case to a legal-aid bureau. It goes without saying that probably few of them have the necessary financial backing to fight a case in court. The seller, on the other hand, either has his own attorney or has retained a legal representative to handle his cases.[2]

A fourth abuse of installment credit is its effect on retail prices. Figures showing the markup common in installment sales have already been given. Variation in prices is concealed by as many as twenty-four different plans in operation. According to the theory of competitive prices there can be only one price at a given time in a given market for commodities of the same quality. This assumes that prices are openly stated so that buyers are able to compare them. As a matter of fact, prices of commodities sold on the installment plan can be compared if one has the time and ability to reduce them to a common denominator; but this is a formidable task and one therefore rarely performed.

Probably the most serious criticism of installment selling as at present operated is the almost complete lack of regulation of finance charges.

[1] Nugent and Henderson, *op. cit.*, p. 94.

[2] Weiss, William S., *How To Keep Out of Trouble*, especially Chapter One, "Beware of the Pitfalls of Installment Buying!," Doubleday, Doran & Co., Garden City, N. Y., 1942; also Public Affairs Pamphlets, No. 61, *Installment Selling—Pros and Cons* by Foster, William Trufant.

From the consumer's point of view it makes no difference whether he borrows $100 from a bank or $100 from a merchant; installment selling merely makes the merchant a banker. Legally, however, there is all the difference in the world, for the bank is restricted by law in the amount it can charge, while the installment merchant can charge any rate he can get. Not only is there no legal regulation, outside of Indiana and Wisconsin, but, as has been shown, there is no effective regulation through competition. This explains the prevalence of such high rates commonly paid for the installment privilege and for the still higher rates which are sometimes paid.

A decade ago the Consumers' Advisory Board of the National Recovery Administration recommended that all lenders be required to reveal the true interest rate in comparable terms. It was recommended that the following provision be included in the finance corporation code,

> "No finance corporation shall accept installment payment from any retailer unless the price differential between cash and deferred payment price be expressed not only as money but as a percentage computed on the basis of the current, unpaid monthly balance of the amount of the installment credit extended. This percentage differential, like the present money differential, may properly include a charge for cost of insurance, where the seller has an insurable interest in the merchandise for which credit is extended."[1]

Unfortunately, installment credit practices and costs cannot be regulated effectively by the simple device of setting a maximum legal rate. Installment finance companies like banks, building and loan associations, and unlicensed personal finance companies, have found that there are many ways to charge interest without appearing to do so. When Utah set a maximum rate on automobile installment sales at 8 per cent " . . . no dealer in the state paid the slightest attention to the law . . . " and when Wisconsin prohibited an interest rate above 15 per cent " . . . many dealers charged about what they would have charged anyway, but did not call it 'interest.' "[2]

Several states have tried regulations but have met with indifferent success. In addition to Utah and Wisconsin, Indiana, Michigan, Maryland, and New York have passed legislation at least for partial regulation. In Indiana and Wisconsin the laws require that the seller give the buyer complete details of the installment transaction in dollars and cents, together with a statement or insurance policy describing the insurance

[1] Foster, LeBaron R., *How Easy Are "Easy Payments?,"* p. 13, Pollak Foundation for Economic Research, Jaffrey, N. H., 1940.

[2] Foster, William Trufant, *Public Supervision of Consumer Credit*, p. 19, Pollak Foundation for Economic Research, Jaffrey, N. H., 1939.

coverage. Indiana licenses all finance companies and requires detailed reports. Maximum rates for carrying charges are set by the state banking department and full-time investigators are employed to be sure that these limits are not exceeded. Installment sellers who do not deal with finance companies are not included in the law. Rates which have been set by the banking department have been so high that it has been possible for most of the dealers to operate at a profit. The Wisconsin law applies only to motor vehicles, but goes much further in that field than does the Indiana statute. In Wisconsin manufacturers, distributors, dealers, and salesmen are licensed as well as the finance company. Regulations are enforceable through the power to revoke licenses, a power which has been used vigorously. There are no rate limits, but the enforcement agency requires each finance company to secure approval of its rates, rebates, fees, and penalties. One weakness of the Wisconsin law, however, is that it appears to have been designed to protect the small business men fully as much as consumers.[1]

Ayres holds that the Indiana act has not accomplished the results hoped for. In order to be effective, says Ayres, the law must regulate both the cash and the time prices. This of course, would require complete price fixing and is therefore unlikely.[2]

In the opinion of Nugent and Henderson installment credit abuses, although common, are not typical of installment selling as a whole. Those responsible for such practices are comparable to salesmen of fake stocks and bonds in the field of investment banking. Seligman contended that there is a tendency for installment prices to fall into what he calls a normal rate, but such inductive evidence as is available scarcely supports this view. Until installment buyers develop more wisdom than they have shown heretofore and more resistance to forceful selling, the installment method of purchasing goods will continue to be unduly expensive.

Is It Wise to Buy on Credit?

Each Consumer Must Decide for Himself. Whether or not a consumer is wise in using his credit to make a purchase is a question which depends on a number of variable factors. One of these is the size of his income. There can be no doubt that for those buyers whose income is large enough to permit them to buy all necessities and a reasonable number of comforts out of income and savings the course of wisdom is to pay cash.

[1] Foster, William Trufant, *Public Supervision of Consumer Credit*, p. 19; Foster, LeBaron R., *Credit for Consumers*, p. 27; Foster, William Trufant, *Installment Selling—Pros and Cons*, p. 27, Public Affairs Pamphlet No. 61, 1941.

[2] Mors, Wallace, "Rate Regulations in the Field of Consumer Credit," in the *Journal of Business*, Vol. 16, April, 1943, p. 137.

Generally speaking the cash buyer gets more merchandise for his money. If his income and rate of impatience are so adjusted as to make it possible to save the purchase price in advance he gains in a number of ways. Instead of paying interest he receives interest on his saving. By having cash on hand he can buy in larger quantities and at opportune times so as to get the lowest possible cash prices. Instead of paying 10 to 40 per cent for the privilege of immediate use, the cash buyer purchasing with his savings may save from 10 to 30 per cent. This is merely another way of saying that for every dollar spent he secures more real income.

Dropping to the next income group, where maintenance of a cash reserve in the form of a bank deposit is either impossible or uncommon, the answer will be somewhat different. In this group family heads will be found carrying fairly substantial amounts of life insurance. In most cases policy contracts covering life insurance carry a loan privilege for reserves. As a general rule it is unwise to borrow on life insurance contracts, for they are to be regarded primarily as a means of protecting dependents against loss of income. Properly regarded and understood, however, a loan on an insurance policy is perfectly legitimate and justified. A family sufficiently provident to use this means of providing for its future is less likely to fall prey to unscrupulous installment salesmen. Neither is it likely to jeopardize the insurance at stake by borrowing too much or for unnecessary commodities. If such a family finds that the opportune time has come for making an addition to needed household equipment or to replace a car whose expense of operation is mounting because of age or wear, it would be far wiser to borrow enough cash on a life insurance policy than to make the purchase on the installment plan. This is a matter of simple arithmetic. A policy loan can be negotiated at the rate of 5 or 6 per cent a year, which is at least 4 or 5 per cent less than the lowest finance charge and as much as 30 per cent less than the highest charge found in Massachusetts.

However, there is one serious defect in this proposal. Under the installment plan the buyer is bound as tightly as legal instruments can tie him to repay the amount of the loan with interest at regularly recurring intervals. The borrower on a life insurance policy is under no compulsion to repay the loan unless a definite program of repayment is followed. It would be easy to permit a loan to run indefinitely. In such a case interest charges would mount and the advantage in such a method of purchasing would be lost.

Dropping to the next income group, where the weekly income is so small as to prevent the purchase of life insurance if an adequate plane of living is to be maintained, there is still an alternative to the expensive method of installment buying. Membership in a credit union makes it

possible to borrow at a rate not exceeding 12 per cent. Increasingly, commercial banks are establishing personal loan departments whose interest charges range from 12 to 17 per cent on declining balances. Loans may be negotiated through Morris Plan Banks at similar rates. Average rates for remedial loan societies are 16 to 22 per cent. For purchases involving $300 or less, consumers in this income group should compare these various rates with finance charges required on the installment purchase plan. In order to make such a comparison the prospective borrower may use the formula on page 272. If the installment purchase costs run in excess of 12 to 20 per cent as they frequently do, it would be wiser to negotiate an outright cash loan to finance the purchase.

It is probably to this group that the largest volume of installment sales are made. And it is for this group most difficult to answer the question whether it is wise to buy on credit. It must be recognized that even though installment buying is expensive it is helpful to consumers in this lower-income group, particularly those who find it psychologically difficult to save in anticipation of a purchase and for whom facilities for saving are limited. For such buyers the installment plan combines immediate satisfaction with incentive and the means to save for payment.

Does Installment Selling Increase Income? Distinction is usually made between producers' and consumers' loans on the basis that while the former use their borrowed purchasing power to secure goods and materials to be refashioned for resale at a profit, consumers must necessarily use their borrowed purchasing power to secure present satisfaction of wants which otherwise would go unsatisfied. Whether or not immediate satisfaction of consumer wants constitutes a productive loan is a moot question. The single distinguishing feature between a productive and a consumptive loan is that the former is self-liquidating in the sense that the income yielded through its use is sufficient to repay it. In the case of a consumer's loan there is no objective test such as profit. The use of borrowed purchasing power may enhance greatly the satisfaction received by a consumer, but it does not necessarily increase his ability to repay the borrowed sum.

Professor Seligman stoutly defended the idea that "Installment credit . . . does not simply advance purchasing power; it may augment purchasing power."[1] He contended that if installment credit renders it possible for a consumer to secure in the present consumption goods which in the long run will increase his productive efficiency it should be regarded as a productive loan. The assumption back of that conclusion is that the consumer borrower enjoys an increasing flow of income.

[1] SELIGMAN, E. R. A., *The Economics of Instalment Selling*, vol. 1, p. 283, Harper & Brothers, New York.

It is that very assumption which appears to be invalid. While it may be true in certain types of occupations where remuneration is based on output, a vast majority of workers receive a stated income per hour, day, week, or month which is unaffected by temporary changes in efficiency. Even in the case of a man working on the piece rate basis it is difficult to imagine that the purchase of a $20 watch for $40 will stimulate his productive efficiency to the point that such a purchase may be regarded as a productive loan. In the words of Roger Babson, "How can the purchasing power of the wage earner be increased by charging him more for what he buys?"[1] On the other hand, it is quite certain that an individual employed as a bookkeeper, salesclerk, or in any one of dozens of other occupations where he is paid by the week or month will not find any possible increase in his efficiency resulting from a consumptive loan reflected in increased income.

In a majority of cases consumer purchases must be paid for out of savings, current income, or future income. For most buyers the installment credit plan is a means of mortgaging future income. This means that what is spent at the present cannot be spent in the future; that for the most part installment buying does simply advance purchasing power. This is a very important thing for consumers to realize. As individuals and as a group, consumers are prone to magnify the importance of goods in the present while at the same time tending to underestimate the importance of cash in the future. It is well to remember that after the first thrill of possession has passed away, the burden of paying for a commodity for eighteen months or even three years is likely to grow from month to month. As the satisfaction derived from the merchandise diminishes, the importance of the cash exchanged for it increases. For every consumer who buys on the installment plan the days of reckoning will come with monotonous regularity. Unless each individual can be reasonably sure of an increasing income in the future he had better balance carefully the present utility of the desired goods with the future utility of the cash exchanged for them. Babson thinks, "It is too bad that we have not had as much money spent in instructing the *consumer* in reasons why he or she should not get intangled in instalment buying. If every dollar spent in urging instalment buying were met with another dollar to point out the disadvantages, I am sure a great many prospective instalment customers would be guided away from the pitfalls of instalment buying."[2]

Should Installment Buying Be Limited to Necessities? There is a popular tendency to deprecate the purchase of luxuries on the installment plan.

[1] Babson, Roger W., *The Folly of Instalment Buying*, p. 12. J. B. Lippincott Company, Philadelphia, 1938. [2] *Ibid.*, p. 60.

This grows out of the common conception noted in the discussion of emulation that persons in the lower-income groups do not have a moral right to any of the comforts or luxuries. These are to be reserved, in the minds of a few, for that small number of persons enjoying large incomes.

As a matter of fact, the term luxury is illusive. Whether regarded absolutely or relatively, the term is difficult of definition. If it is defined as a free indulgence in costly gratifications of the appetites or tastes, the usual presumption is that the costliness confines it to those able to pay. Obviously the definition itself is relative. What constitutes a luxury for one person may logically be regarded as a necessity for another. By the same token commodities regarded as luxuries at one time become necessities at a later period. The automobile is probably the best illustration of a rich man's toy becoming a poor man's necessity for transportation.

Whether or not the consumer borrower's earning power is increased by the purchase by the installment method of a commodity which some may regard as wanton luxury, may be a debatable question. But as long as consumers have any semblance of freedom of choice it is unwise and probably futile for one group in a favored position to condemn another group for succumbing to the insistent demands of advertisers, salesmen, and installment merchants that they buy now and pay later for the things they would like to have.

Summary

Buying implies the exchange of goods and services for cash in possession of the buyer. But a buyer may give a promise to pay, in lieu of cash. About one fifth of retail sales involve credit, and about one third of those credit sales involve the installment credit plan. Ordinary credit is used for convenience and to meet emergencies. Installment credit is primarily a means of supplying consumers now with goods they would ordinarily have to wait for until sometime in the uncertain future. This involves considerable additional cost, which varies among commodities. Advantages of the system include enjoyment of goods while paying for them, compulsory saving, and possibly a tendency to encourage wiser use of income. Offsetting abuses include the use of installment credit as a means of forcing sales of illth or nealth; many fraudulent practices have developed and sellers are overly protected by legal instruments; finally, there is little or no regulation of finance charges in most states.

Broadly speaking, it is unwise and uneconomical for consumers to buy on the installment credit plan. But this is a subjective matter, depending on size of income and rate of impatience. If credit is needed it can usually be secured from other agencies at a lower cost. For most buyers installment purchasing cannot increase income; it simply ad-

vances purchasing power. As long as credit is being used there is no good reason for limiting it to any special type of merchandise.

QUESTIONS FOR DISCUSSION

1. What is credit? What are its various forms?
2. Have you ever purchased goods on the installment plan? If so, why? Do you know what it cost? If not, why not?
3. Is your rate of impatience high or low?
4. What are the costs of installment credit? How can you calculate them?
5. Are installment credit costs too high?
6. What are some abuses of installment credit? Can you cite illustrations from your own experience?
7. Is it wise to buy on credit?
8. Does installment credit increase income?
9. Does installment credit increase sales and lower prices, as some finance companies' advertisements imply?
10. Should installment buying be limited to necessities?
11. An automobile is priced at $600 after down payment. If you wish to buy it on the installment plan the carrying charge for 12 months is $36. What is the cost rate you will be paying for installment credit?

PROBLEMS AND PROJECTS

1. Make a credit survey of your home community, or of the one in which you are now living. Take one or several of such items as food, clothing, coal, furniture, household appliances, or automobiles, and ascertain from merchants what proportions are purchased on credit.

2. What are the costs of installment credit in your community? What do they cover besides interest charges? Make a study of installment credit prices for a selected group of articles, comparing them with cash prices. This project may be combined with Project 1 above.

3. Ask a selected group of consumers whom you know and who make use of credit why they buy on credit; inquire whether they are aware of the additional costs of credit, particularly on the installment plan. Classify and tabulate your answers.

4. What sources of consumer credit are available to buyers in your vicinity? Have commercial banks developed personal loan departments? Do you have a Morris Plan Bank? A Credit Union? A branch office of a Personal Finance Company? A pawnshop? Make a study of the comparative methods used by these agencies and their costs.

5. Secure from local installment merchants copies of the legal instruments used in making an installment sale. Find out what percentage of installment merchandise is repossessed; and what the repossession costs are. To what extent are wage assignments used in your community?

Part Three

MAKING CONSUMER CONTROL EFFECTIVE: A TECHNOLOGY OF CONSUMPTION

15

Consumer Education

Consumers Need Education for Living

The Complex Business of Living. One's views on consumer education will vary with one's views as to the place and function of consumers in the economic system. Is their function that of guiding and controlling production of goods with which to satisfy their wants? Or is their function that of serving as tools for profit-seeking producers who actually guide and control production of economic goods? If one takes the first view the ultimate test to apply to all production is consumer welfare. But if one takes the latter view the final test is whether production of specific goods will yield profit. According to the first view questions will be raised as to whether commodities commonly accepted as wealth are really wealth, or nealth, or illth (page 52). Similar questions will be raised concerning methods of marketing. Proponents of the latter view, however, will raise none of these questions. If commodities produced and methods of marketing them are profitable their first concern will be to maintain the *status quo*.

In Parts One and Two, the theory of consumer control of the economic system has been examined. According to this view consumers are supposed to guide production. To a large extent they fail to perform this function, and to the extent to which they do fulfill their part they do it badly. They do not know for certain what they want, nor do they know how to get what they think they want. They are influenced by custom, and desire to show off or to copy; by fashion, advertising, and high prices; they are easy victims of those who practice fraud or misrepresentation; with decreasing resistance they succumb to the lure of installment selling. As a result considerable waste detracts from genuine consumer welfare.

The obvious and underlying reason for this situation is that consumers are uninformed. But why are consumers uninformed? Why do they not know what types of goods and services are good for them? Why are they so susceptible to such influences as those just mentioned? If living is the most important thing consumers do, why are they not trained in the art of living? Why is there hardly any consumer education in a country so devoted to the principle of mass education? There is a vast difference between education in general and educating consumers in the art of living. Reading, writing, and arithmetic in the elementary grades, and sciences through secondary schools, colleges, and universities, are taught primarily as working tools rather than as consuming arts. Neither family, nor school, nor government, nor church has undertaken genuine education of consumers for living. One significant educational agency is business, which, through advertising, has undertaken an extensive campaign to educate consumers. Its main objective, however, is that of making profit rather than that of promoting the welfare of consumers. In this one educational project business spends as much in one prosperous year as consumers annually appropriate for general education.

Reasons for Lack of Consumer Education. If consumers are not fully informed concerning methods of the market place, why have not educational agencies attempted to inform them? Why is it that this particular phase of education has not been developed more extensively? A number of reasons may be advanced. One of these is the legal doctrine of *caveat emptor*. According to this doctrine of law which prevails in the present economic system the buyer should beware when he enters the market place. Unless he can prove subsequently that a seller made express warranties concerning mechandise sold, a buyer has no redress at law. Obvious defects are covered by this maxim, it being presumed that a buyer, having opportunity to examine whatever he purchases, is able to discover any defects, and for subsequent disillusion he has no one to blame but himself.

The doctrine that buyers should beware developed historically sometime subsequent to the Middle Ages. Medieval records reveal extremely minute regulations designed to protect the consumer. A court case in 1625 involving purchase of a worthless stone marks the rising tide of the doctrine that buyers should beware, in the absence of an express warranty at the time of the sale. With the subsequent rise of individualism, encouraged by the writings of Adam Smith, the doctrine of *caveat emptor* fitted perfectly. Its greatest triumph has been realized in the United States. Under the Federal constitution and the state constitutions certain fundamental property rights such as private property and freedom of contract are guaranteed. Only when exploitation of consumers be-

comes too extreme is it possible for a government to intervene, using its police power. In many cases even that is not permissible, such devious devices as the Federal power to regulate interstate commerce or the power to tax being required to circumvent constitutional restrictions. As a policy restricting any activity designed to inform or protect consumers, *caveat emptor* is still very real and contemporary. "Business is business and law is law, but neither insures quality," style, or durability in any commodity. Under this doctrine the business of buying is a game of chance. The individual consumer goes into the market place as a lone wolf, there to meet the collective onslaught of salesmen and advertisers whose sales talks are not limited to statements of fact. Against their determination to make him buy something he neither wants nor needs he has only his senses as his guide and protector.[1] The counterpart of this doctrine is that known as *laissez faire*. Practically all businessmen believe in this doctrine that government should in no way interfere with business. Its strongest adherents will readily accept governmental aid but protest bitterly against governmental aid to consumers, which they regard as governmental interference. Between the upper and nether millstones of *laissez faire* and *caveat emptor* it is small wonder that American consumers have had little education in the art of buying.

A second reason for lack of consumer education is the popular belief that consumers somehow will learn the art of living as they grow up, without any special training. The similarity between economic and political literacy and illiteracy has been suggested previously. Politically and legally individuals are regarded as irresponsible infants until they reach age 21, or some earlier age, as 18. Then suddenly and mysteriously with no special training they are presumed on a certain day in their lives to be capable of assuming and carrying out their political or legal responsibilities. In the economic sphere a similar presumption prevails with the exception that no special age limit is recognized as marking attainment of economic literacy. Like Topsy, consumers are supposed to grow up and, having reached the physical proportions of manhood or womanhood, to be able to assume economic responsibilities. Individuals do learn, after a fashion, how to buy. Somehow they muddle through. But they are likely to acquire an exaggerated concept of the simplicity of their functions as consumers. It is, after all, but a simple thing to spend money; what is not simple is to learn how to spend money wisely.

A third influence lying back of failure to educate consumers is the predominance in American thought of the belief that consumer welfare is best advanced by increasing individual income. This is quite in har-

[1] Hamilton, Walton H., "The Ancient Maxim—*Caveat Emptor*," in *Yale Law Journal*, June, 1931, pp. 1133–1137.

mony with an acquisitive philosophy. If one has ample income, failure to spend portions of it wisely will not be serious. Even though wealthy consumers do not get their money's worth in the market place no serious result follows, for they have enough to supply all legitimate needs. The difficulty is that so few consumers are wealthy. If a $2,000 income is unwisely spent so as to yield but $1,800 worth of satisfaction, whereas it could have been made to yield its full equivalent, a definite individual loss has been incurred. This simple fact has been ignored too long. Instead of teaching consumers how to maximize the utility of their incomes they have been taught that the way to increase their welfare is to increase their incomes. There is no reason, of course, why both methods may not be used, but if one is to be used to the exclusion of the other it would be far better to emphasize consumer education, for the possibility of achieving immediate results is probably greater than the possibility of enhancing income. As things stand, we have reared generations so engrossed in the task of earning that they have had no time to devote to the art of living.

Why Modern Consumers Need Special Training. Half of the national income is spent by consumers over the counter. If such items as taxes, medical costs, rent, fuel, light, club and lodge dues, and other such expenditures are included the amount of national income spent by consumers is raised to 80 per cent.[1]

With the exception of very small children, everyone in the family shares in this buying process. From the time small children are old enough to be sent to the store until the end of their lives most of their satisfactions are secured through the buying process. Yet there is very little formal training for this activity. What the average buyer does not know about the things he buys is appalling. Yet there has been almost no response on the part of educational agencies to the growing need for special training.

There are at least three reasons why the need for consumer education is greater than formerly. For one thing, there is more buying to be done as specialization increases. In contrast with colonial families, modern urban families are compelled to buy practically everything they use. Under colonial agricultural economy practically all food was raised by the family and prepared in the family kitchen; sheep raised on the farm yielded wool from which yarn was spun and woven into cloth; surrounding forests yielded logs and lumber with which houses were built and much furniture was made. A modern rural family is still somewhat self-sufficient, but even agriculture has become specialized and farmers

[1] U. S. Dept. of Interior, Office of Education, *Consumer-Buying in the Educational Program for Homemaking*, Vocational Education Bulletin, No. 182, p. 4.

increasingly rely on the market place for things they need. Very few modern farm homes are built with lumber grown and sawed on the premises; nor are they furnished with homemade furniture. The larger part of farm clothing is purchased in stores, and an increasing amount of food is supplied commercially. Dependence of the modern urban family on the market place is practically complete. Food, clothing, shelter, furniture, almost everything, is bought. Yet these modern consumers receive no more formal training in the art of buying than their ancestors, and probably receive less informal training within their family circles.

Not only is there more buying to be done, but the pressure to do it is very great. New gadgets and devices made to catch the eye are placed before potential buyers whose resistance is broken down by specialists in that task. Against the scientifically planned attacks of salesmen, fortified by advertising and easy payment plans, modern consumers have been unable to develop a defense.

Not only is there more buying to be done and more pressure to encourage consumers to do it, but there are also more goods among which consumers must choose. A partial list of commodities available to present-day consumers but which were unknown to their ancestors includes the whole array of electrical appliances such as lights, fans, refrigerators, and toasters, modern heating systems, automobiles, telephones, and moving pictures. Even though real income may be larger, the task of apportioning it among many more commodities is difficult. All consumers would like to have these modern comforts and luxuries, and the efforts of some to acquire them are an indication of lack of training in the setting up of objectives designed to promote real and permanent welfare.

Not only are there more goods to be bought, but there are also more brands among which to choose. When consumers go into the market place, on what basis shall they decide which of many brands of identical merchandise to purchase? Operation of competitive forces has resulted not in one or even a half dozen competing brands, but in scores or hundreds. The chief educational device for informing consumers is advertising. Yet obviously all brands cannot be the best even though their makers claim such superiority. With two or three notable exceptions, not one of the other educational agencies has made any effort to provide consumers with an objective basis for choosing among brands. That the need for such training is growing is shown by the results of a survey in Milwaukee. The number of brands of the nineteen products listed in Table XXIII on page 290 increased in six cases from 1939 to 1942 and in seven cases from 1942 to 1943, in spite of war restrictions.

The United States Department of Commerce made a survey of St.

TABLE XXIII.—THE NUMBER OF BRANDS AMONG WHICH MILWAUKEE FAMILIES HAVE TO CHOOSE[1]

Product	*Number of Brands*		
	in 1943	in 1942	in 1939
Package coffee	80	115	127
Canned corn	—	193	184
Baked beans	—	56	51
Peanut butter	98	97	107
White bread	25	30	29
White flour	62	61	53 (1938)
Regular milk	42	37	35
Ice cream	24	28	—
Toilet soap	74	75	81
Roll toilet paper	—	136	153
Tooth paste	77	71	83
Tooth brushes	207	—	223
Liquid shampoo	175	170	170
Mouth wash	116	112	124
Safety razor blades	168	174	198
Washing machines	—	133	144
Portable radios	—	55	38 (1940)
Cigars	162	—	235 (1938)
Cigarettes	37	36	

Louis drugstores. It was found that an active drugstore carried in stock 7,838 different items. Duplicate brands of items in a single store included 312 laxatives, 132 antiseptics, 111 cold creams, 87 face powders, 77 cough syrups, 53 toilet soaps, 44 hair tonics, 44 shaving creams, 41 tooth pastes. To the extent that the Milwaukee and St. Louis surveys are typical they emphasize consumers' need for special training in the technique of buying.[2]

Type of Training Required. The type of training which modern consumers need is general rather than technical. Human wants and the goods to satisfy them are far too numerous and complex for individual buyers to develop expertness in choosing. Since women do so large a part of national buying, these functions, in addition to their other numerous duties in operating the home, require so much time that it would be impossible for them to test every purchase. Other limitations to such expert buying would include lack of knowledge, interest, and equipment. Moreover, most women do not have enough money to spend to enable

[1] *The Milwaukee Journal*, *War-time Consumer Analysis*, 1943.

[2] For further discussion of this topic see TONNE, Herbert A., *Consumer Education in the Schools*, chap. 2, "The Need for Consumer Education," Prentice-Hall, New York, 1941; also BUSH, George L., *Science Education in Consumer Buying*, chap. 1, "The Need for Consumer Education," Bureau of Publications, Teachers' College, Columbia University, New York, 1941.

them to buy in large enough quantities to justify testing. It may be that an individual housewife can make a good spray or silver polish by purchasing the ingredients and mixing them in her own kitchen. But such jobs are messy and take considerable time for one unaccustomed to them. The net result is that very few consumers can or will undertake to solve their problems in that way. After all, individual housewives should be able to buy good sprays and reliable silver polish in the market place at a reasonable price. The ultimate hope of the consumer does not lie in the possibility of making every individual an expert buyer, but rather in the realization of their collective function and power.

The first thing which consumers need to know is their part in the economic system. The motivation and operation of that system need to be explained and understood. Consumers must be acquainted with its virtues as well as its defects. They must understand that the persistence of fraud, misrepresentation, and other undesirable practices is possible because of their own lack of organized resistance. Consumers need to realize the importance of substituting rationality for emotion in the market place. The manner in which such forces as custom, fashion, and advertising cause them to act against their own self-interest needs clarification.

A second step in the general training of consumers requires that they be informed and made aware of their need for developing themselves as wise consumers. The main task here is to combat the prevalent idea that the way to achieve consumer welfare is to increase individual income. Consumers need to be made consumer conscious, and to realize the possibility of thus enhancing their income as consumers. It is imperative that consumers develop a realization of their need for protection from certain current practices. One reason so many frauds are successful is because consumers are so blissfully unaware that certain predatory producers would resort to such practices to secure a profit.

If and when consumers begin to realize these first two objectives, the third essential of this program of general training will be apparent. By that time consumers in large groups will be convinced of the necessity for active organization of consumers' groups. These organizations may take several different forms, ranging from small neighborhood groups to organized political action. As individuals, consumers are helpless, but as well-organized groups they can exercise effective influence. They can, in short, guide and control the economic system.

Once consumer groups are organized their next step should be to seek positive aids in their attempts to develop themselves as wise buyers. The educational program should include the determination of standards of wise consumption which will promote their welfare. Obviously, if

individuals do not know what is good for them they are severely handicapped in any effort to play the part of a rational consumer. These consumer organizations can insist upon other such positive aids to economical buying as standards of quality. Price without a specification of content and quality is meaningless, yet in large part that is the basis on which consumers now buy.

These consumer organizations will find it necessary to insist that the state use its power to restrict certain undesirable economic practices. Since every housewife cannot test all of her canned goods, electrical appliances, or whatever else she buys, it is important that housewives collectively support a demand for modern laws requiring minimum standards for certain goods. In the same manner housewives can determine the future of advertising. They can assure its continued growth and profitableness by letting it sway them as at present; or, by ignoring all but truthful, informative advertising they can make all other advertising fail to pay. As a middle course, consumers' organizations can demand laws requiring advertisers to limit their statements to positive information.

Agencies for Educating Consumers

The Family. An agency which should be one of the most effective in consumer education is the family, but at present its influence in that field is largely negative. Children are highly impressionable in formative years and they acquire, by precept and teaching, economic habits which will govern their actions as consumers throughout life. Most parents are poor teachers, having had no special training as consumers and lacking interest in developing wise consuming practices. Such family practices as shopping by telephone, maintaining charge accounts, relying on newspaper, magazine, and radio advertisements, buying on the installment plan, and failing to budget income are perpetuated through imitation by children. "Life's failures are found among those who never learned how to earn, how to spend, or how to save wisely."[1]

There are at least four fundamentals which family training could and should include. First of all, the sources and amount of family income should be known to each member. One of the first important lessons which children need to learn is that money is obtained by expenditure of effort; that its acquisition requires physical or mental exertion. Probably the most effective way of impressing this fact on youthful minds is to provide children with opportunities for earning money. If that is impossible or impracticable, children should be placed on an allowance

[1] Blodgett, Harvey A., *Making the Most of Your Income*, p. 112, by permission of The Macmillan Company, publishers, New York, 1933.

with a clear understanding concerning its limitations and uses. This will develop a realization that money is limited; that its utilization is necessary to secure maximum satisfaction; that not every passing fancy can be gratified.

The next step in family training for wise consuming should include co-operative planning in spending the family income. This calls for making a family budget in which every member of the family except very small children should join. This will teach the older children the benefits to be derived from planning expenditures and will lead them ultimately to budget their own income. Upon reaching maturity and when establishing homes of their own, they will continue this fundamental of wise consuming as a matter of habit. One obstacle to complete use of budgeting is the failure of one of the senior partners in a family to co-operate. The result is not only failure to maximize present family income, but also failure to transmit a wise practice to youthful consumers.[1]

Youthful consumers should be taught to pay as they go. One of the most valuable lessons which parents can teach their children is the general rule to pay cash for whatever they buy, or to go without until they have the cash. Much unhappiness results from efforts to stretch a limited income farther than it will go. Individuals should learn at an early age that unless they have unlimited incomes they cannot satisfy every want. Efforts to do so will lead only to dissatisfaction. Children reared in families who joke about installments due develop an unfortunate attitude toward this important question. The extent to which excessive costs of installment buying diminish family real income has been shown in Chapter 14.

Buying is an art which needs to be taught and developed as any other art. Not many parents let their children learn to swim by throwing them into deep water and letting them sink or churn their way out. Yet this is practically what most parents do in teaching their children to buy. When the weekly order of groceries is to be purchased, youthful members of the family should accompany the one who does the buying to observe the technique. Like apprentices of old, these children will see how mature buyers shop from store to store, comparing price and quality to the extent of their ability. They will see the savings to be made by paying cash. In the buyer's pre-shopping preparations they will learn how to use available buying guides. In seeking to secure the best quality at the lowest price they will learn not to ignore the wages and working conditions of those who made the merchandise. Socially minded consumers do not wish to benefit at the expense of fellow-consumers.[2]

[1] For a suggested technique of budgeting see Chapter 16.

[2] For helpful suggestions to wise buyers see Chapter 17.

A significant by-product of this type of family consumer education would be the practice of democracy in family life. In most families today there is probably much less exercise of parental authority than in former generations. This does not mean, however, that every member in the family shares and has a voice in family government. An excellent point at which to begin is family rather than purely parental decision as to how family income shall be spent. Recognition of the right to share in control and practice of that right would provide future generations of Americans who would be better consumers and better citizens.

These comments on family training are suggestive rather than inclusive. They indicate in broad outline form the great possibilities of the family as an institution for training consumers in the art of living. Although the faculty is large it is poorly trained. If this agency alone were responsible for educating consumers the prospects of developing a nation of economic adults would be discouraging.

Schools. Americans firmly believe that free, compulsory education is the basis of intelligent democracy. In the face of this conviction it is all the more strange that formal educational practice has so largely ignored education for consumers. While this curious anomaly may be explained, it cannot be justified. A fact too frequently overlooked is that the American system of free, compulsory education is only a century old. In the radical 1840's a few minority groups, including labor unions, demanded free public education. As the system developed, courses to be taught were adopted in accordance with the prevailing idea that if children were taught how to earn money they would somehow learn how to spend it. As a result the prevailing tendency in teaching basic subjects was to emphasize them as tools for securing and holding a job. By contrast, the curricula of private colleges and universities whose student body was drawn largely from well-to-do middle-class or wealthy families aimed to provide a cultural education. Between these extremes there was no provision for educating the masses in the art of consuming.

Dominance of boards of education by businessmen has perpetuated what was started. Their chief concern is usually with "practical" subjects, that is, with teaching young men and women how to earn money by running a business. Modern boards of education, similarly dominated by businessmen, object to what they regard as the debunking aspect of consumer education. Any proposal to educate consumers of necessity runs counter to this view. Roger Babson thinks that failure to teach the danger and damage of installment buying is an outstanding bare spot in the American educational system. He recognizes, however, that such a topic would arouse a storm of controversy if introduced into school courses. Any teacher who tried to expose the evils of installment buying,

says Mr. Babson, would incur the wrath of local installment merchants and would be subjected to relentless pressure from many sources.[1]

It is argued that since business pays the taxes which support the schools it is unjust to use these funds to teach consumers how to buy wisely. The assumption on which this view is based, that business pays all or most of the taxes, will scarcely stand analysis. While this is not the place to discuss tax theory, it may be noted that many, if not most, business taxes are ultimately shifted to consumers. In the final analysis all taxpayers are consumers, and with the rapid spread of sales taxes nearly all consumers are taxpayers. As such, they have a legitimate right to insist that a portion of the tax receipts be used for consumer education.

The power of custom goes far to explain the relative fixity of educational curricula. Colleges call it tradition and are inclined to regard it with reverence. In elementary or secondary schools or institutions of higher learning once a curriculum has been adopted it tends to become fixed even though economic conditions out of which it developed may change. Such changes have occurred and call for a change in curricula. Yet custom fortifies other forces in opposing a change designed to promote consumer welfare.

What can the schools contribute to consumer education? When the change eventually comes, what changes should be made in courses and methods of study? Few if any fundamental changes are necessary. Consumer education can be developed within the framework of present curricula. It should supplement rather than displace current courses of study. The chief requirement is a shift in emphasis in teaching certain basic subjects, such as English, mathematics, basic sciences, social studies, and commercial subjects. The objectives should be to use these courses of study as means for developing wise standards of consumption and presenting a technique of buying and use. English reading courses should recognize and include the literature of consumer education. The study of mathematics should include buying projects for teaching the use of fractions, while the mysteries of insurance could be clarified by problems dealing with actuarial aspects. Sciences, particularly chemistry and physics, could be vitalized by teaching their uses to consumers in testing quality. Social studies, particularly economics, government, sociology, and psychology, could serve as media for educating consumers concerning their place and function in the economic and social order. Particular emphasis could be placed on individual and social forces playing on consumer desire.

In recent years there has been a significant growth in the number of

[1] Babson, Roger W., *The Folly of Instalment Buying*, p. 113, J. B. Lippincott Company, Philadelphia, 1938.

courses dealing with home economics. The chief limitation at present is that these studies appeal mostly to girls. While this is desirable since women do so large a part of national buying, it is also important to impress boys with the necessity of assuming their share of responsibility. Probably this can be accomplished best through other courses less commonly regarded as feminine. An illustration of the possibilities of extending traditional home economics courses to include buying and analysis of products is found in the experience of Miss Isabella F. McQuesten, a teacher in the Union High School at Phoenix, Arizona. Objectives of the project were to acquaint students in a food management course with legislation and other helps for buying food. The large number of food products available was emphasized in several ways. Each member of the class reported on dishes served on previous days. The class then grouped the articles of food according to frequency of use and type. Class members visited grocery stores and noted the number of different brands of a particular food, while others selected a specific food to investigate the forms and qualities available in the market, such as pineapple, which can be bought sliced, crushed, as tidbits, as juice, and in broken slices. Some students observed a particular part of the grocery store to discover less frequently made food purchases, while others took unusual foods such as canned pickled peaches to discover in what type of menu these could be used economically. They considered also when it would be unwise to buy these types of food.

In an effort to discover what helps are available and their usefulness to food buyers, the project included a study of labels, grades, advertisements, salespersons, and brands. Considerable time and emphasis were spent on this phase of the project, including an analysis of the informational value of labels, the relative use to buyers of descriptive as compared with letter labeling and grading, a test of salespersons' knowledge of their products, and several subprojects dealing with food advertising.

A third main feature of the project was the study of Federal governmental aid to the buyer of foods. Beginning with the Food and Drug Administration other Federal bureaus offering help to food buyers were studied, such as the Bureau of Human Nutrition and Home Economics. The project was concluded with a panel discussion on ways in which the Federal and state governments could render further services to consumer buyers of food.[1]

[1] *Consumer-Buying in the Educational Program for Homemaking*, p. 47. For further suggestions see Tonne, *op. cit.*, chaps. 6, 9, 10, and 14; Institute for Consumer Education, *Next Steps in Consumer Education*, Stephens College, Columbia, Missouri, 1939; *Making Consumer Education Effective*, Stephens College, Columbia, Missouri, 1940; *Consumer Education for Life Problems*, Stephens College, Columbia, Missouri, 1941; National Education Association of the United States and the American Association of School

Government and Consumers. Since consumers are the largest body of citizens it might be supposed that governmental agencies would function first and primarily in their interest. This might be true if consumers knew what they wanted and were well organized, but in fact the supposition ignores the influence of small and well-organized groups. For example under the National Industrial Recovery Act codes were to be drafted jointly by representatives of industry, organized workers, and consumers. In practice most of the codes were written by legal and expert representatives of the industry so as to include not only all the provisions the producers wished to include, but many more which could be sacrificed for bargaining purposes in subsequent hearings. In the hearings representatives of organized labor were present, and sometimes representatives of consumers. There was, however, no considerable representation of consumers, for the simple reason that there are few consumer organizations. To remedy this situation the administration appointed consumer representatives. The chief function of these, as well as of labor representatives, was negative. That is, their task was to point out the more glaring assaults on the rights of consumers and workers, leaving them practically no opportunity to offer constructive suggestions.[1]

A few of these early New Deal consumer agencies survived, and one, the Consumer Counsel Division, in the Department of Agriculture, gradually developed increasingly educational functions. Together with the Bureau of Human Nutrition and Home Economics, The Consumer Counsel Division became increasingly important in the growing consumer movement. Consumer representation in the Federal government reached its peak in 1940 when a Consumer Commissioner was appointed to serve as one of the seven members of the Advisory Commission to the Council of National Defense. But in less than a year that separate representation was abolished to become a part of the Office of Price Administration and ultimately to be discontinued. Since that time the Consumer Counsel Division has disappeared and the only agency performing significant consumer educational services is the Bureau of Human Nutrition and Home Economics.

Administrators, Educational Policies Commission, *Education and Economic Well-Being in American Democracy*, Washington, D. C., 1940; CLARK, Harold F., Editor, *Economic Education*, National Council For the Social Studies, Washington, D. C., 1940; BOYCE, George A., and RISANDER, A. C., *Social-Economic Mathematics*, Copyrighted and published by the authors, Bronxville, N. Y., 1936; MERGENDAHL, Charles H., and FOSTER, LeBaron R., *One Hundred Problems in Consumer Credit*, Pollak Foundation for Economic Research, Pamphlet No. 35, Jaffrey, N. H., 1938; MENDENHALL, James E., and HARAP, Henry, *Consumer Education*, especially chaps. V through XVI, D. Appleton-Century Co., New York, 1943.

[1] For an authoritative account of what took place see CAMPBELL, Persia, *Consumer Representation in the New Deal*, The Columbia University Press, New York, 1940.

As a result of this situation consumers are practically where they started. Today governmental aid to consumers is limited and usually incidental. It is amazing but true that neither in the Federal government nor in any state government is a single department devoted to consumers. By contrast the United States Department of Commerce is assiduously alert on behalf of businessmen, while the Department of Labor devotes its attention to promoting the welfare of organized workers. An indication of the educational work now being carried on by governmental agencies, together with suggestions as to what can and should be included in a governmental program for educating consumers, will be found in Chapter 27.

Adult Study Groups. Latent possibilities of adult consumer education are very great, but obstacles to achievement are numerous and deeply rooted. Agencies for educating adult consumers include Consumer Information Centers, Co-operative Associations, the American Home Economics Association, the American Association of University Women, National League of Women Voters, National Consumers' League, and local consumer study groups. The chief limitations to effective achievement are fear, inertia, lack of time, and lack of interest. Opposition of business groups on which family heads are dependent for income makes many consumers hesitate to associate with such groups. Real or imagined lack of time renders it difficult to plan and carry through a program of consumer education. Long working hours for those gainfully employed, and the still longer hours and numerous duties of housewives, leave but little if any time or energy for such study groups, whose beneficial effects are frequently difficult to measure.

In spite of these difficulties, adult consumer education is growing. By this means the interest of consumers in their particular problems is aroused and developed. Collective and co-operative action strengthens their demands for consideration. By studying particular projects, members of these groups are informed concerning prices, quality, and business practices. Reports on pending legislation are prepared by experts. These make possible intelligent support or opposition on an organized rather than on an individual basis. Local groups undertake projects relating to their immediate problems. It was such a group of housewives that conducted tests of canned vegetables described in Chapter 13. Individual experiences are compared and group pressure can be brought to bear on recalcitrant local dealers. Suggestions for consumer education for adults will be found in Chapter III of *Consumer-Buying in the Educational Program for Homemaking.*

The Church As an Educational Institution. In the past the church as an institution has not been actively concerned with economic questions.

Such matters as those involving the business of living have been regarded as beyond the area of religious education, yet problems involving personal morals such as liquor consumption, gambling, and vice have been regarded as proper spheres for expression of church attitudes. By some religious groups war has been included in this category. While these problems have their economic aspects they have not been so regarded by church members.

Certain notable developments have occurred which require that the church be included definitely as a possible educational agency and force for consumers. The successful campaign of churches, regardless of denomination, through the National Council of Decency in securing higher standards on the part of moving-picture producers is an illustration of this attitude. In that campaign the church definitely assumed the role of an educational agency, using the long-familiar weapon of boycott to enforce its demands. In recent years certain Protestants, particularly the Methodist denomination, have become concerned with the attitudes of church members toward social and economic questions. Traditional objection to the use of intoxicating liquors, to gambling, vice, and war, is maintained but finds a new basis in its social consequences. Consumers as church members are being taught that they should be concerned not only with low prices but with wages and conditions of work imposed on those who labor to satisfy consumer wants. Unchristian aspects of the profit motive are being emphasized. Church members are being told that they as producers cannot continue to dupe consumers and still consider themselves Christians. Perhaps most notable of all is the recent interest in and support of the co-operative movement by certain denominational groups. This movement is supported as a definite way of Christian living. Increasingly the church is being committed to the view that religion must deal with current social and economic questions. In this the Federal Council of Churches of Christ in America has taken a leading part. The chief educational function of the church at present and in the future will be that of guiding consumers in formulating standards of welfare. Rarely will the church assume the role of educating in the technique of consumption.

Business As an Educational Force. Business has been and is an active educational agency. Judged on the basis of achieving its objectives, business education of consumers has probably been more successful than that of any other agency. The main objective has been to induce consumers to act the way producers wish. This means there is a vast amount of competitive educational work. In the very nature of things every consumer cannot function as every producer would like. With limited incomes if consumers buy more of one kind of goods they frequently

buy less of another, while the very nature of competing brands renders it impossible for them to use more than one at a time. Nevertheless, regarding business as a whole, its efforts to educate consumers to their way of thinking have been successful. Through advertising, control of the press and radio, and influence in schools, the business point of view has been predominant. This is emphasized by noting the rapid growth in the number of schools of business. Yet this type of education is less needed than is consumer education. A successful English businessman has expressed the view that "There is no need to spend public money on the teaching of such things; on the contrary, it would be better to teach the public to resist the blandishments of salesmen and advertisers."[1]

By contrast not a single school devoted exclusively to consumer interest has been established. Financed by the Alfred P. Sloan Foundation, the Institute for Consumer Education was established at Stephens College in 1937. It was expected "to give impetus to the consumer approach to economic teaching, to aid in co-ordinating the work being carried on in the subject, and to act as a clearing house for information regarding courses of study, research, and publications in the field." Three national conferences of consumer educators were held at Columbia, Missouri, in 1939, 1940, and 1941. The Institute did give impetus to the consumer movement, so much so, in fact, that certain non-consumer interests objected vigorously. The Institute started to decline in the middle of 1940 and without public announcement it was discontinued early the following year.

Through Chambers of Commerce and other such organizations businessmen have been successful in securing governmental aid. This is reflected in the large number of governmental services performed for business in contrast to the much smaller number of services performed for consumers.

An interesting analogy can be drawn between leaders of business and certain religious leaders. In some cases the latter have objected to enlightened members and have sought to maintain their traditional power by using a language unknown to all but themselves. Thus in Turkey, until a few years ago, Arabic was the official Moslem church language known only to church officials. Only since about 1930 have Mohammedan Turks been able to recite their prayers in a language they understand. In a similar way most business leaders object to enlightened consumers. Any proposal for presenting positive information in simple terms is regarded with alarm. Curiously enough, businessmen do not

[1] Courtauld, Samuel, "An Industrialist's Reflections on the Future Relations of Government and Industry," in *The Economic Journal*, April, 1942, p. 11, Macmillan & Co., Ltd.

object when they or their competitors act as economic men. When they go into the market to purchase commodities they pay little if any attention to exaggerated advertising claims. They maintain purchasing departments manned by experts. Orders are placed, on the basis of competitive offers, for merchandise which must meet the buyer's specifications. Yet any effort to teach ultimate consumers to act as economic men is resisted vigorously.

In the long run this system of deliberately maintaining ignorance among consumers is shortsighted. Legitimate business has nothing to fear from enlightened consumers. Those who have much to fear and whose opposition is strongest are those whose stock in trade is consumer credulity. For men of vision and courage willing to use their advertising to give consumers reliable, worth-while information there is a great future. Businessmen now spend as much per year to educate consumers as is spent by all public schools. If these vast financial resources were to be used in a way more helpful to consumers, business would become one of the most significant, positive educational agencies. As it is, business is a powerful educational force, but one whose efforts are directed too largely in the wrong direction.

An example of the type of intelligent business education proposed by businessmen is to be found in the recommendations of The Twentieth Century Fund Committee on Distribution. That Committee was composed of Willard L. Thorp, Director of Economic Research for Dun & Bradstreet; Stuart Chase, Economist; Alvin Dodd, President, American Management Association; John P. Frey, President, Metal Trades Department, American Federation of Labor; Hector Lazo, Executive Vice-President, Co-operative Food Distributors of America; Paul Nystrom, President, Limited Price Variety Stores Association; Robert G. Stewart, Standard Oil Company of New Jersey; Carl L. Hamilton, and Helen Hall. After agreeing that marketing does cost too much, the Committee recommended the following specific policies:

1. The expansion and better co-ordination of government agencies to provide in adequate and popular form information which consumers need for more efficient buying.

2. There must be even greater achievement toward the elimination of fraud and misrepresentation in printed and oral descriptions of products.

3. Informational labeling must be more widely used by sellers.

4. Businessmen should establish a differentiated pricing system for retail goods. This would make it possible for consumer-buyers to break down the charges for delivery services, return privileges, credit, telephone, special shopping service, etc.

5. There should be a wide expansion for public use of the facilities of government and of private agencies for testing and appraising consumer goods. They expressed the conviction "That the Bureau of Standards should make tests of leading products for specific qualities and that the results should be made public."

6. They urged the further organization of consumer co-operatives and consumers' group buying agencies.

7. The extension and further development of courses on consumer problems in educational institutions is strongly recommended.

8. The final proposal calls for an increasing number of studies dealing with family budgets and expenditures.[1]

Prospects for Educating Consumers

Very Great Possibilities. The possibilities of consumer education are virtually unlimited. On paper one can solve all consumer problems by building up a program of education. If consumers were properly educated as consumers, they would know what goods they want, would be able to judge quality and price, and consequently would guide the entire economic system so as to yield maximum consumer welfare. If consumers were educated, a large part of the waste now resulting from their unenlightened choices would disappear. If consumers were educated, the power of custom in life would diminish, leaving them freer to choose goods calculated to promote their well-being. If consumers were educated, they would disdain a vulgar display of pecuniary power. While fashion would not disappear, its extreme hold on individual consumers would be diminished, to their advantage. If consumers were educated, much of modern advertising would be ineffective, for emotional appeals cannot withstand the cold light of rationality. Advertising would not disappear but would be revamped so as to become a helpful guide for wise buyers. If consumers were educated, they would know that high price is no measure of quality. They would know that except in rare instances they should buy only for cash and that where credit is required it can be secured elsewhere more cheaply than through the installment system. If consumers were properly educated, the profitable practice of fraud would be seriously deflated. They would know that they cannot buy health or beauty in bottles or jars prepared for sale by untrained, irresponsible, predatory producers.

Practical Limitations. All these problems and many more could be solved by education, but if one wishes to treat consumer problems realistically it must be recognized that they cannot be dismissed with a simple statement that what is needed is education. Such an attitude

[1] Stewart, Paul W., and Dewhurst, J. Frederic, *Does Distribution Cost Too Much?* pp. 350–354, The Twentieth Century Fund, New York, 1939.

merely restates the problem. That problem is how, if at all, are consumers to become educated? The baffling truth is that uninformed consumers are not aware of their credulity. Consequently, they are not aware of their need for education and are therefore not interested in efforts to give it to them voluntarily. If attempts are made to meet this obstacle by compulsory education, opposing interests block that way out. A report issued by the American Association of University Women contains a statement which epitomizes this situation.[1] "Many who started out enthusiastic over the possibility of consumer education are becoming convinced that the scarcity of subject matter which is of definite value and the diversity and nature of commodities to be purchased combine to limit the efficacy of this method as a sole means of providing the help needed in the purchase of a specified article." It is recognized, however, that education can make a buyer more cautious and rational, thus preventing such gross errors in judgment as characterize current consumer choices.

Consumer education is growing on several fronts. The negative aspect of family and business consumer education continues, but in schools, government, adult groups, and to some extent in the church, consumer education is expanding. By its very nature progress will be slow. In the meantime, that small vanguard concerned with achieving genuine consumer welfare will seek to accomplish their objective by supplementing efforts to secure consumer education with efforts to help ultimate buyers in other ways. The following chapters will deal with some of these other methods.

Summary

Although the art of consuming wisely and well is a prerequisite for consumer welfare, no educational agency other than business has made a serious effort to teach consumers how to play their part. Unfortunately, businessmen's education of consumers is largely negative. This situation results from the doctrine of *caveat emptor*, the belief that consumers can learn by experience alone, and the idea that consumer welfare is promoted most effectively by attempting to increase individual income. Modern consumers' need for special training is increasing because there is more buying to be done, the pressure to do it is greater, and there are more products and brands among which to choose.

The type of training needed is general rather than technical. Within the family infant consumers should be taught the meaning and value of

[1] O'Brien, Ruth, and Hartley, Olive, *An Analysis of Consumers' Facilities for Judging Merchandise*, p. 6 (*op. cit.* on page 244).

money, how to budget income, and how to buy. In the public schools and universities consumer education can be developed within the framework of existing curricula by shifting the emphasis and changing the method.

By consolidating its activities the Federal government could give great impetus to the movement for educating consumers. For those who are beyond the formal school system, adult education groups can be devoted to consumer training. There is a tendency for some church denominations to broaden the scope of their activities to include education of consumer members along special lines. Through advertising, business has assumed a major role in training consumers; but that training is designed to make consumers act for the benefit of sellers rather than for their own welfare. The possibilities of consumer education are very great, but practical limitations are so serious that this device must be supplemented by other aids to consumer welfare.

QUESTIONS FOR DISCUSSION

1. How does the theoretical compare with the actual function of consumers in current economic life? How well do you play your part as a consumer?
2. What agencies might educate consumers? Which ones have been most active? Why?
3. Why is there so little consumer education in primary and secondary schools?
4. Do you as a modern consumer need any special training?
5. Outline a statement of objectives for a program of consumer education.
6. How much training as a consumer have you had in your family life? When you have a family of your own, what kind of training will you attempt to provide for its members?
7. How much consumer education did you have in primary grades? In secondary schools? Outline a plan for expanding this type of training in the public schools.
8. In your judgment should the church attempt to assist in educating consumers? If not, what are your objections? If you think so, along what lines should such a program be developed?
9. Can all the problems of consumers be solved by education?

PROBLEMS AND PROJECTS

1. Write a paper on the legal doctrine of *caveat emptor*.

2. Interview ten representative businessmen in your community; ascertain the extent of their knowledge of consumer education; then tell them what it involves and secure their reactions.

3. Ascertain how much was spent in your county or state for public education last year; compare that figure with the amount spent for commercial advertising.

4. Write a report, based on one issue of a nationally circulated magazine, showing how much educational material is included in the advertisements. Is it positive or negative, that is, designed to benefit buyer or advertiser?

5. Prepare a short paper on the consumer activities of the National Council of Decency or the Federal Council of Churches.

6. In collaboration with a student specializing in education draw up a plan for introducing a comprehensive program of consumer education in your local public schools.

7. Make a survey of two or three food and drug stores to find out the number of brands of several items carried in stock.

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Planning Expenditures: Budgeting

Family Income and Spending

The Family As an Economic Unit. Just as the corporation is the unit of organization for production, so the family is the unit of organization for consumption. In order to produce wealth in the modern way men find it necessary to combine their productive resources in some form of business enterprise. In colonial days, whose simple economic life has been described, the most common form of business organization was that in which a single individual organized a business in which land, capital, and the labor of others were combined under his direction. A second form of organizing for production is the partnership in which two or more men combine their resources. From the standpoint of profit making certain disadvantages of these two forms of business organization, such as unlimited liability and uncertainty of life, led to their displacement by a new form of organization known as the corporation. This change began to take place in the period following the Civil War. It has continued until now approximately 90 per cent of all wage earners are employed by corporations which produce 92 per cent of all manufactured products, and add to raw materials in process of manufacture 91 per cent of all value thus added in American factories.

While these extensive changes have been taking place for producing wealth no comparable changes have occurred in the unit of organization for consuming wealth. The family now, as in colonial times, is the economic unit around which consumption is organized. While men as producers have experimented with several forms of organizing for business they have not as consumers experimented with any other form of organization than the family. It is true that the number of families has increased until now their number is ten times that of the total population in the colonial period. In 1942 there were approximately 41,000,000 civilian spending units in the United States. These consisted of 33,000,000 families of two or more persons and 8,000,000 single civilians maintaining independent living quarters or living as lodgers or servants in private homes, rooming houses, or hotels.[1]

[1] Office of Price Administration, Division of Research, Consumer Income and Demand Branch, *Civilian Spending and Saving, 1941 and 1942*, March 1, 1943, p. 4.

Also there has been a significant shift in population from country to city which has had a modifying effect on family life. Apartment-house living has changed the family as a consuming unit in some ways. The central heating plant has replaced the individual fireplace, stove, or furnace; janitor and maid service are included in the monthly rental. In recent years there has been a noticeable encroachment by business organizations on functions formerly regarded as essential features of family life. Thus bakeries, canneries, creameries, and laundries have assumed economic tasks previously performed by the family. In this way the family has become less and less a producing unit and more completely and exclusively a consuming unit.

So it is that the 33,000,000 families in the United States are primarily consuming units with no more, and in many cases much less, practical preparation for their duties than that possessed by their forebears. On the other hand, they are subjected to a much greater pressure by producers than their ancestors ever knew. So we find this striking contrast: that as the unit of production has become more specialized and more efficient the unit of consumption is no more specialized and probably less efficient than formerly.

While the family is the dominant consuming unit, the "lady of the house" is the most important member of that unit, for her position as the family's purchasing agent is firmly established. In the year 1942 it was estimated that American women spent $56,000,000,000 as consumers. As the heads of family consuming units, women buy 80 to 90 per cent of all merchandise purchased for family use. Specifically, they buy about 96 per cent of all dry goods, 87 per cent of raw market products, 48 per cent of hardware and furnishings, 48 per cent of all drugs, and 41 per cent of the automobiles. Nor is this all. Women buy about 11 per cent of men's clothing and ties without consulting the men, and assist in selecting 23 per cent more.[1]

Women have very little preparation for their responsibilities as purchasing agents. Whereas a business is established to make profit and employees are hired on the basis of efficiency, the family is founded on love, and the matter of efficiency in no way regulates its composition. Men do not usually marry women because they are efficient homemakers

[1] Frederick, Mrs. Christine, *Production from the Viewpoint of the Consumer*, pp. 134–135, in Frederick, J. George, *A Philosophy of Production*. A recent estimate made by Isabel Everett, "Who Buys the Family Groceries," in *Journal of Home Economics*, vol. 32, pp. 96–98, gives considerably different figures. Her survey, made in January and February, 1939, in three high schools in Wilmington, Delaware, revealed that the women of the 215 families studied made 50.8 per cent of the total purchases of groceries; the men 10.4 per cent; men and women together .5 per cent; children from 15 to 18 made 27.5 per cent of the purchases, and children under 15 were responsible for 10.8 per cent of the purchases.

and careful spenders. Moreover, the task of purchasing for a family is vastly different from that of purchasing for a business organization. The purchasing agent for the latter has one task to perform on which he can specialize, while the range of commodities which he has to buy is limited to those required by that particular business. The purchasing agent for a family, on the other hand, finds that her task of buying is only one of many which must be taken in the full stride of a day's work. Also the range of commodities which she has to buy covers the whole field of human wants and includes practically everything ready for final consumption. Finally, women do not approach their task of buying in a professional spirit. In business efficient methods are spread by competition, but in the home that method is less likely to operate, for a family usually resents being told how to do a thing more efficiently. Such competition as does take place is likely to take the form of competitive wasteful spending.[1]

To the extent that these observations are true it is all the more essential that members of a family co-operate in spending the family income. Just as corporation officials must co-operate to secure maximum profit, so family officials must co-operate to secure maximum utility. A budget supplemented with a record of expenditures is the key to co-operation in spending family income wisely.

What Is Income? Every week, two weeks, or month the family provider, who serves the dual role of producer and consumer, receives wages or a salary in the form of money, check, or some other form of claim on wealth. For purposes of distinction money may be described as any universally acceptable medium of exchange, while a check is an order by one person, on a bank in which a deposit has been made, to pay a third person. Since the value of checks depends upon the credit of the drawer and of the bank, they are not usually acceptable media of exchange in distant places or among strangers. Other forms of claims on wealth may include scrip and store orders. Do money or these substitutes for money constitute income? In a limited sense and in popular concept they do, but actually they are useless in themselves. It is only when they are translated into real income by exchanging them for goods and services that they assume significance. A money income of $30 a week contributes to human welfare only to the extent that it can be exchanged for such things as food, clothing, and shelter. If prices are high, a $30 weekly money income shrinks considerably when translated into real income, while it may expand if prices are low. Economists measure these variations in purchasing power of money by a device known as an index

[1] Mitchell, W. C., "The Backward Art of Spending Money," in *American Economic Review*, vol. 2, pp. 269–281.

number. Taking 1935–1939 as base years, indexes of the retail cost of food in large cities rose from 93.5 in August, 1939, to 139.0 in July, 1943. This is to say that in 1939 a $30 weekly money income would buy as much food as $32 would have bought in the base years, while in July, 1943, prices having risen, $30 would buy only as much food as $21.58 would have purchased in the base years.

The concept of income may be carried a step further. The wealth which money will buy is in itself useless if not consumed. It is only when wealth is actually consumed and yields its services to members of the family that income is realized. When a part of the $30 is spent for shoes, the shoes themselves do not constitute income; the income is derived, rather, as the shoes are worn. Of the three kinds of income so far discussed this is the most real of all and is called by economists psychic income. Although it is the most real form of income it is the least measurable because of its subjective nature, and consequently has received scant attention.

Income in kind consists of receipt of goods and services directly as wages or for which no cash outlay is required. If the family with a money income of $30 a week has a garden plot which yields vegetables throughout the summer the vegetables constitute income just as truly as though part of the $30 had been spent to purchase them. The $30 income is augmented by the amount which the vegetables would have cost in the market. When a mathematician teaches mathematics to an artist and the artist teaches the mathematician the elements of straight-line drawing, both are enjoying income though no money is involved. If a family owns the house which it converts into a home, the services of that house day by day constitute income though no direct cash outlay is required. In all these cases there is a cost involved, however. This will be shown particularly in the case of a house in Chapter 22.

In this chapter the concept of money income will be used. Budgeting money income will be presented as a means of spending so as to maximize its utility.

With increasing specialization in production women and younger members of the family have gone into industry to earn money which is pooled and becomes part of the family income. Consequently, the concept of family income is of more significance than that of individual income. If the $105,000,000,000 received by the 41,000,000 civilian spending units in 1942 had been divided equally among them, each unit would have had an average money income of about $2,560. Actually, each of 16,700,000 families received less than $1,500 in that year. These families were about 41 per cent of the total number, yet they received only about 14 per cent of the aggregate money income. This group was

able to purchase only 19 per cent of total consumer goods and services. For families with an average income of $862 the average outlay was $845. They were barely able to maintain even their usual low living standards out of current income. In fact, a substantial portion of this group spent more on current living than they received as income, thereby going into debt or liquidating assets. The group with incomes between $1,500 and $3,000 contained 34 per cent of the nation's spending units. This group received 28 per cent of the aggregate income and made 33 per cent of the total consumer expenditures. With an average income of $2,139 their average consumption expenditure was $1,763. Putting these two groups together, it is seen that 75 per cent of the spending units in 1942 received only 42 per cent of the money income.[1]

It must be remembered that the total figures for money income in 1942 are abnormally high and they represent an increase of about 21 per cent—$18,500,000,000—over 1941. The 1941 figures, in turn, were higher than those for 1940 and 1939. Although incomes went up 21 per cent, 12 per cent of that increase was absorbed by higher personal taxes. Consumption increased 15 per cent, while savings increased 71 per cent. As a result of rising prices, aggregate consumption in 1942, measured in 1941 dollars, was actually lower than in 1941.[2]

When compared with any one of the several estimates of the amount of money necessary to maintain a family of four on a decent standard of living, it is evident that for millions of families incomes are so small that extremely careful planning is needed to make them yield maximum utility. While the achievement of economic welfare waits upon the production of more wealth and a more equitable distribution of wealth produced, a long forward step can be taken by improving the methods of utilizing income now received. Budgeting income is probably the first step toward such improvement.

How May Income Be Used? The question as to how income may be used may appear superfluous. What is money income for, it may be asked, if it is not to be spent? But what constitutes spending? Is there a difference between spending and saving? What shall we say about income which is given away? Is it proper to speak of that as being spent? Suppose one hoards, or loses, or throws away income. Shall these be considered as spending?

The first and most obvious use of money income is to spend it, if the spending is defined as the exchange of money for consumers' goods or services. Consumers' goods may be bought for immediate use and may, like bread, be completely used up in the process of satisfying

[1] *Civilian Spending and Saving, 1941 and 1942*, *op. cit.*, pp. 4–7.
[2] *Ibid.*, pp. 1–2.

wants. There are other consumers' goods whose use is prolonged over a period of time. These may eventually be used up in the sense that they are worn out and incapable of further satisfying wants. Such goods, like antique furniture, may be called durable consumers' goods and may last through generations of families. Among the 16,700,000 family spending units whose incomes in 1942 were less than $1,500, it has been seen that their average money income was $862, of which $845 was spent for current consumption.

Among those families whose incomes are large enough to meet minimum standards of living and leave a surplus over and above immediate needs, the surplus may be saved. Among the 800,000 families and single civilians receiving $10,000 and over in 1942, 31 per cent of the money received was saved. Saving may be defined simply as the postponement of consumption. That is, surplus money is exchanged for some form of wealth or claim on wealth which yields more income currently and in the future. Instead of being spent for food, clothing, radio, or vacuum cleaner it may be spent for a business building, stocks, bonds, or insurance. These items of wealth or claims on wealth are expected to yield supplementary income now and in the future.

Why do people save a part of their income? One reason is to provide for their old age. Although it is estimated by the Social Security Board that, of the 8,600,000 people who are 65 years of age or over, 5,200,000 are dependent, many of them have attempted to provide for their old age during their productive years. Another reason for saving is to prepare for emergencies such as illness and unemployment. The full shock of the business depression which began in 1929, with its subsequent unemployment of millions of workers, was not felt until late in 1932. This was partly due to the fact that some families affected by unemployment had maintained themselves by using their savings. Closely related as a reason for saving is the desire of family heads to provide for their dependents after the Grim Reaper has passed. While saving for that contingency takes many different forms, probably the most common is that of insurance. The importance of insurance is shown by the 50,000,000 to 70,000,000 policyholders whose problems in buying protection will be discussed in Chapters 20 and 21. Another reason why people save is to provide the means for educating children and for travel. Many students are in college because someone has saved. The pleasures of travel have been opened to millions of consumers in recent years by the production of low-priced automobiles. Another reason why a small group of people with very large incomes save is because their incomes are so large that even though they resort to the most conspicuous forms of consumption they cannot possibly spend all the money which comes into their pos-

session. While this list of reasons why people save is not intended to be complete, it does include the most important reasons lying back of the determination of families or individuals to postpone their consumption.

Is saving spending? To most people to whom the distinction between saving and spending is not clear, it seems that saving is not spending. The brief discussion thus far should make it clear that saving is a form of spending, differing from other spending in the character of the goods received for the money income. When an individual or family spends a dollar for food or medical services the money is spent for immediate use. But if the dollar is deposited in a savings account or applied towards the purchase of a bond it would be spent for future use. In either case the money is exchanged for something else. Control over it passes out of the hands of the one who spent it. The difference lies in the type of goods for which the money is spent. Realization of the true nature of saving will go far to dispel the popular belief that saving is not spending, and that it takes money out of circulation.

A third way in which money income may be used is to give it away. A considerable amount of money income is redistributed through contributions. The first type of gift which comes to mind is probably that of a father to his children. More striking cases are those in which a man of wealth transfers large fortunes to his children before his death in order to escape payment of inheritance taxes. There are about 56,000,000 people belonging to the various churches in the United States, whose buildings number 211,000 and are valued at $3,400,000,000. If these members were to practice the Biblical injunction of tithing their incomes, a significant percentage of national income would be given to churches each year. This suggests a purely parenthetical thought. When tithing was first advocated as a religious practice it was popularly believed that a 10 per cent contribution represented an equal sacrifice by all contributors. Centuries later the study of economics revealed the principle of diminishing utility. In more recent times the principle has been extended to include money. By combining the principle of diminishing utility with the facts of unequal distribution of income, the conclusion may be reached that the individual or family whose annual income is $1,000 is sacrificing a great deal more by giving $100 to benevolences than is the family which contributes $100,000 out of an income of $1,000,000. Modern taxation recognizes this principle and applies it in the form of the progressive income tax.

Money income may be used by giving it to philanthropic, charitable, and educational institutions. In 1940 there were 314 philanthropic foundations and funds in the United States. The total capital assets of 162 of that number amounted to $1,073,500,000. During the year the

gross expenditures of the foundations were approximately $51,000,000, of which $40,000,000 represented grants. It is estimated that 30 per cent of the foundation grants were for the study and promotion of medicine and public health, 29 per cent for education, 11 per cent for social welfare, 10 per cent for physical and biological sciences, 4 per cent for social sciences, and 3 per cent for religion.[1] While the contributions of millions of small-income receivers are not so apparent they are nevertheless very substantial. In fact one survey led to the conclusion that it is the contributions of the so-called middle-class families which constitute the backbone of American philanthropy.

A fourth and final way of using income is to hoard it or throw it away. Neither of these is spending, and neither is sufficiently important to justify a further discussion.

If the family income is not to be frittered away or squandered, if its utility is to be maximized, its expenditure requires careful planning. The best way to plan is to budget; in fact, planning expenditures is budgeting.

Budgeting As a Plan for Spending

Planning Versus Budgeting. The family head or housewife who does not in some measure plan future expenditures must be rare indeed. Probably most consumers plan their expenditures in advance after a fashion. There are very few who can afford to spend spontaneously without thought. Some adults as well as children are economic infants who spend haphazardly and with abandon, and whom we call spendthrifts; but they are not common. The planning of most consumers, however, is likely to be in the nature of unconscious planning of regularly recurrent expenditures, with deliberate planning only in the case of larger unusual expenditures. Installment buying has helped those making use of it so to plan their expenditures as to be able to meet their installments. In a limited sense it may be said that such planning is budgeting; but as the term is used here, budgeting is the drawing up in written form of a complete plan of spending for a definite period in advance.

Functions of a Budget. A definite plan for spending in advance yields a number of beneficial results. Unlike a business organization, a family has no measurable test like profit with which to measure the utility of its expenditures. The objective is family welfare, which is difficult if not impossible to measure. In the absence of a specific test a budget is a valuable means of comparing various items in family expenditures. By committing anticipated expenditures to paper, the important ones will

[1] Seybold, Geneva, *American Foundations and Their Fields*, pp. 4, 5, 37, Raymond Rich Associates, New York, 1942.

be made to stand out more sharply when compared with the less important. The process of budgeting is more likely to insure provision of essential goods and services. With the aid of sample minimum budgets two measurables are provided: maximum income and minimum needs.

A second advantage of budgeting is that it thus becomes a device for promoting rational instead of irrational use of income. The very act of drawing up the budget promotes a more careful evaluation of consuming standards. Such evaluation tends to elevate the importance of utility in choosing goods and services, at the same time minimizing the influence of fashion and of what one's neighbors are doing. To the extent that rationality thus displaces irrationality in consuming, those persons who budget their incomes approach the concept of the economic man.

Budgeting is beneficial also to the extent that it facilitates the balancing of irregular income against regular expenditures. It is much easier for a family receiving a regular monthly income to plan its expenditures informally than for a family whose income is intermittent. Wage earners, commission men, and businessmen dependent on profits can never be certain of their annual income. The wife of a workingman receiving $30 a week should not budget on the basis of $1560 a year. If her husband is a coal miner he might best plan on no more than forty weeks' work, which would bring only $1,200 a year. A commission salesman may earn $500 one month and $100 the next two months, giving him an average of $200 a month. In the absence of a budget there would be a strong temptation to spend on a $500 scale during the first month, which would require spending on a $50 scale in the other two months. Wives of businessmen dependent on profits are still more uncertain as to what their annual income will be, for the profit of $500 in December may be offset by a loss of $500 in August. If the family were to live on a $500 scale in December they would have to draw on savings or borrow to tide them over the month of August. All of this may be summarized in the observation that the minimum amount necessary to maintain the desired plane of living is fairly regular (ignoring long-time changes in price levels), while for many families not only the time of receipt but also the amount of annual income is uncertain. A family budget based on past experience will go far toward eliminating this uncertainty.

Another service which budgeting may perform is that of facilitating the adjustment of expenditures to increased or decreased family income and to increased or decreased family size. It is a commonplace that in our machine economy the man who earns his livelihood by manual labor enjoys his maximum income in the years from 20 to 40. Beyond 40 years of age a worker begins to slow down and his earnings decrease,

till eventually they approach zero. For those whose income permits a margin of saving, budgeting helps to prepare for the lean days ahead. For those whose incomes are too small to permit the maintenance of a decent plane of living, to say nothing of saving, the problem of care in old age becomes a social rather than an individual question. On the other hand, professional men and businessmen may with some assurance anticipate an increased income in the years from 40 to 60 or 65. A knowledge of these facts, together with a program of budgeting income in the lean years, will assist toward a maximization of utility throughout the whole period. Budgeting is beneficial also in those cases of sudden, unexpected increases or decreases in family income. During war boom days when some people enjoy unexpected increases in income, failure to budget may lead them into a scale of living which cannot be maintained in the lean years which are likely to follow. Wives of salaried men who find their real incomes reduced as money prices rise, as well as the wives of workers whose incomes decline in depression years, are better able to adjust themselves to such reductions if they operate on a budget.

A family passes through three distinct cycles in its development. In the first one to three years following marriage the family usually consists of only two, so that even a modest income may be budgeted to include some comforts and a few luxuries. As children begin to arrive, there follows a period, lasting until perhaps twenty years after the birth of the last child, in which the expenses of the family are increased, and unless the family income is increased proportionately, which is rare, a reallocation of expenditures must take place. The third period is that following the maturity of the children, when they are no longer dependent. As they leave the family home to set up their own homes, the size of the family is decreased, and unless the family income decreases proportionately, which also is rare, there is left to the parents a larger amount to be used in other ways. Throughout these three periods of family history the wise use of a budget will facilitate the adjustment to changes which are inevitable.

A fifth advantage to be gained by the use of a budget is that it makes possible a comparison of expenditures for selected items. It thus becomes possible to determine whether the allowance for each item is more or less than that in comparable approved minimum standards. A proper budgetary allowance not only for food but for certain kinds of food will promote health as well as yield organic utility. The same generalization applies to other items in the budget. By comparison with sample budgets, housewives may learn not only that approximately 9 per cent of their income should be budgeted for clothing, but they may discover also how much should be allowed for specific articles. A sample budget will

reveal that the cost of shelter should approximate 15 per cent of the income, but it will also describe what the householder should receive in the way of rooms and facilities.

A sixth function of budgeting is to discover and plug leaks in family expenditures. It is a common experience of all who have money to spend, to discover to their utter amazement that within a short time after receiving wages or salary check it is impossible to recall where or for what a portion of it was spent. If a budget is kept, the records will show what became of every dollar. If any money has been spent foolishly the record will show it, and will help the budgeter to prevent a recurrence.

Limitations of a Budget. Obviously keeping a budget does not enlarge the money income, though it may increase its utility. Those consumers who refuse to be hampered in their expenditures by a budget are really hampered by the size of their incomes. There is no good reason why they may not seek to increase the utility of their money incomes at the same time that they seek to increase the number of dollars in their income.

While the keeping of a budget does not offer any assurance that goods will be chosen wisely, it does operate in that direction. It is quite possible that a family may budget its income very carefully, yet the budget may include unimportant or even harmful items.

Obstacles to Budgeting. While there is no reliable evidence, that which is available leads to the conclusion that a very small proportion of consumers operate on a budget. In view of the theoretical and demonstrated advantages of budgeting, why is it that the family which thus uses its income rationally is so rare? Certainly one reason is to be found in the intangible results. The most illiterate worker and careless spender can see and feel $2 more a week in his pay envelope. If his wife so budgets his regular $30 wage as to make it yield $32 worth of utility that is much harder to see or measure. Yet the latter may be much more real than the former, for if prices have risen 10 per cent while the money wage has increased by $6\frac{2}{3}$ per cent the $32 will buy less than was formerly obtainable with the $30.

The power of inertia is a tremendously deterring force. The sheer effort of working out a budget and of keeping a record of expenditures is simply too much for many consumers.

Lack of co-operation explains the failure of many families to budget. If either one of the senior partners in a family enterprise refuses to co-operate, budgeting is impossible. As a matter of fact, as the children grow older their co-operation is necessary also. Budgeting is essentially a family project. Each member of the family should have a voice in determining the amount to be spent for all items, whether he contributes

to the money income or not. By the same token each member of the family must co-operate in keeping a record of expenditures. Failure of any one member of the family so to co-operate is disastrous to any budgeting effort.

For those whose incomes are irregular, budgeting is somewhat more difficult. Although the task is harder, the gains are likely to be greater. Yet irregularity of income is an obstacle which deters many families from budgeting.

There may be other obstacles which might be mentioned, but running through and underlying all of them is the fact that American consumers are still primarily production-minded. They still think that the only way to improve their economic welfare is to increase their money incomes. Prolonged periods of depression not only dispel any hope of increasing income, but require the most careful planning to secure the maximum utility of whatever income is available. Likewise, a period of rapidly rising prices such as usually accompanies war, decreases the purchasing power of all those whose incomes are stable. It is then that the household managers of such families find the budget a helpful means of stretching their shrinking dollars. In both of these situations the result may well be the breaking down of former obstacles to the practice of operating a budget.

Technique of Budgeting

Three Steps in Budgeting. The formal process of budgeting income has three separate steps. The starting point is the written plan of expenditures for a definite period in advance, usually a year. This is supplemented by a written record of expenditures during that period, separated by months. The third and final step in budgeting is a monthly comparison of expenditures with the budget allowance.

Drawing Up a Budget. Consumers wishing to increase their real incomes by budgeting will seek some guide in planning their expenditures. One who has never budgeted might easily be at considerable loss to know just how to proceed in the actual setting up of accounts. For such consumers the actual experience of 60,000 families living in cities of different sizes, in villages, and on farms in thirty different states as revealed in their expenditures for the fiscal year 1935–1936 will be useful as a guide. On the basis of the actual experience of the 60,000 families statisticians have been able to provide average patterns of consumption for all American families. These patterns are presented in Table XXIV on pages 318–319.[1]

[1] United States Department of Labor, Bureau of Labor Statistics, *Monthly Labor Review*, vol. 50, p. 379.

TABLE XXIV.*—AVERAGE OUTLAY OF AMERICAN FAMILIES BY INCOME LEVELS, 1935–36

(Estimates of National Resources Committee based on the Study of Consumer Purchases)

Item	All families	Families with incomes of: Under $500	$500 to $750	$750 to $1,000	$1,000 to $1,250	$1,250 to $1,500	$1,500 to $1,750	$1,750 to $2,000
Per cent of families	100.0	14.2	12.9	14.6	13.2	9.8	8.0	6.4
Average income	$1,622	$312	$627	$874	$1,120	$1,364	$1,612	$1,829
Per cent of income for:								
Savings	10.1	†−51.9	†−14.6	†−6.6	†−2.8	1.0	3.5	5.0
Food, total	28.8	65.0	49.5	43.5	38.7	35.7	32.7	30.5
Purchased	24.4	50.0	36.5	34.3	31.9	29.5	27.9	26.8
Home-produced[1]	4.4	15.0	13.0	9.2	6.8	6.2	4.8	3.7
Housing, total	15.3	28.9	19.9	18.5	18.1	16.9	16.6	16.5
Money expense	10.4	19.9	13.5	13.2	12.7	11.6	11.5	11.8
Imputed value[2]	4.9	9.0	6.4	5.3	5.4	5.3	5.1	4.7
Household operations	10.0	18.2	13.5	12.1	11.6	10.9	10.3	10.2
Furnishings	2.9	2.9	2.5	3.1	3.4	3.5	3.5	3.7
Clothing	8.7	11.2	8.9	8.9	8.9	9.0	9.1	9.0
Automobile	7.0	4.8	4.5	5.0	6.3	6.8	7.6	8.4
Transportation other than automobile	1.0	1.0	.8	1.0	1.0	1.0	1.0	1.0
Personal care	1.7	2.9	2.2	2.1	2.1	2.0	2.0	1.9
Medical care	4.0	7.1	4.7	4.3	4.2	4.2	4.4	4.3
Recreation	2.5	1.9	1.7	1.9	2.2	2.3	2.6	2.7
Tobacco	1.6	2.9	2.3	2.2	2.0	2.0	1.8	1.8
Reading	.8	1.3	.9	1.0	1.0	1.0	.9	.9
Formal education	.9	.6	.5	.5	.6	.7	.7	.8
Gifts	2.8	2.0	1.6	1.8	1.9	2.3	2.5	2.7
Personal taxes[3]	1.5	.6	.3	.2	.3	.2	.2	.2
Other items	.4	.6	.8	.5	.5	.5	.6	.4

* Discussed on pages 317–320. † Deficit as a per cent of income.

[1] For method of imputing money value to home-produced foods, see *Consumer Expenditures in the United States*, pp. 94–95. These figures cover rural families only.

[2] For method of imputing money value to owned homes, see *Consumer Expenditures in the United States*, or Bureau of Labor Statistics Bulletin No. 642, vol. II, pp. 230–231.

[3] Taxes shown here include only personal income taxes, poll taxes, and certain personal property taxes.

One value of Table XXIV is that prospective budgeters can look in the column whose family income corresponds most closely to their own and thereby share the experience of several thousands of other families in budgeting their limited income. In the seventh column of the table, for example, the one for families having an income ranging from $1,500 to $1,750, it will be seen that they spent 32.7 per cent for food, 16.6 per cent for housing, 10.3 per cent for household operation, 3.5 per cent for household furnishings, 9.1 per cent for clothing, and 7.6 per cent for owning and operating an automobile. The combined expenditures for

TABLE XXIV.—AVERAGE OUTLAY OF AMERICAN FAMILIES BY INCOME LEVEL, 1935–36.—(*Continued*)

(*Estimates of National Resources Committee based on the Study of Consumer Purchases*)

Item	*Families with incomes of*							
	$2,000 to $2,500	$2,500 to $3,000	$3,000 to $4,000	$4,000 to $5,000	$5,000 to $10,000	$10,000 to $15,000	$15,000 to $20,000	$20,000 and over
Per cent of families	8.4	4.5	4.0	1.4	1.7	0.4	0.2	0.3
Average income	$2,221	$2,715	$3,394	$4,391	$6,874	$11,353	$17,331	$41,871
Per cent of income for:								
Savings	8.2	11.6	15.6	20.6	29.5	38.9	39.9	50.7
Food, total	27.8	25.4	22.7	19.4	15.1	10.7	10.3	5.4
Purchased	24.9	22.8	20.5	17.9	14.1	10.3	10.0	5.3
Home-produced[1]	2.9	2.6	2.2	1.5	1.0	.4	.3	.1
Housing, total	15.7	14.9	14.3	13.0	11.4	10.6	8.6	6.5
Money expense	10.9	10.1	9.6	8.6	7.5	7.0	5.2	3.5
Imputed value[2]	4.8	4.8	4.7	4.4	3.9	3.6	3.4	3.0
Household operations	9.6	9.6	9.4	9.1	8.5	6.7	6.8	5.2
Furnishings	3.4	3.1	3.0	2.5	2.3	2.0	1.6	1.1
Clothing	9.3	9.4	9.3	9.3	8.1	7.3	7.3	5.2
Automobile	9.0	8.9	8.5	8.7	7.6	6.0	5.3	4.2
Transportation other than automobile	1.0	.9	.9	.8	.7	1.0	2.3	1.0
Personal care	1.9	1.8	1.6	1.5	1.3	1.0	.9	.6
Medical care	4.1	4.0	3.9	3.6	3.6	2.0	2.4	2.0
Recreation	2.8	3.0	3.1	3.1	3.0	3.0	2.8	2.2
Tobacco	1.7	1.5	1.4	1.2	.9	.7	.6	.3
Reading	.9	.8	.8	.7	.6	.5	.4	.3
Formal education	.9	1.1	1.1	1.3	1.2	2.0	3.1	1.2
Gifts	2.9	3.3	3.6	4.2	4.3	4.5	3.8	2.1
Personal taxes[3]	.3	.3	.4	.6	1.4	2.9	3.6	11.8
Other items	.5	.4	.4	.4	.5	.2	.3	.2

[1] For method of imputing money value to home-produced foods, see *Consumer Expenditures in the United States*, pp. 94–95. These figures cover rural families only.

[2] For method of imputing money value to owned homes, see *Consumer Expenditures in the United States*, or Bureau of Labor Statistics Bulletin No. 642, vol. II, pp. 230–231.

[3] Taxes shown here include only personal income taxes, poll taxes, and certain personal property taxes.

these six items accounted for practically 80 per cent of the family income. It will be observed that there is very little difference in the percentages of income spent for these six items in the families having incomes ranging from $1,000 to $3,000 annually.

These figures suggest that as a starting point in budgeting one's income the more common regular expenditures to which the family is committed may be budgeted first. These will include the six items listed above and will absorb some 70 to 80 per cent of the family income. As money income increases, the experience of others shows the percentage

spent for food will decline considerably. Likewise, the percentages spent for housing and household operation will decline. Although the percentage spent for clothing declines, the differences between lower and upper income groups are never very large. The remaining 30 to 20 per cent of family income can then be allocated among the eleven other items listed in Table XXIV.

It will be observed that the percentages of income absorbed by taxes in the year 1935–36 were fractional for most of the income groups. It was not until family income averaged $6,874 annually that taxes exceeded one per cent. Since 1935–36 this item in family budgeting has changed drastically. By 1943 taxes had become a significant item in family budgets. Under the withholding income tax then in effect, a married man with two children receiving $30 a week would have $1.20 withheld from his weekly pay envelope. In the professional income level a family head with two children receiving $250 a month would have $18.80 withheld from his monthly pay check.

This suggests two things with reference to effective budgeting. The first one is that certain essential expenditures should be grouped together and placed first in the budget. The second suggestion is that instead of budgeting ten or twelve items, the budget will be far more satisfactory if there are fifteen or twenty items. The fewer the "other items" of expenditures the more accurate and the more useful the budget will be. In Table XXV will be found a suggested budget form. It is difficult to say that some expenditures are essential and others less essential or nonessential, but an effort has been made to group the twenty-three items in somewhat the order in which they should be met. This should not be taken to imply that in case retrenchment becomes necessary certain items would be discontinued completely, but rather that expenditures on some of the essential items might be cut somewhat while less essential items could be cut drastically and nonessentials could be eliminated. The monthly columns are reserved for recording the amounts actually spent so that on one page the budgeter can compare the amount allotted for each account with the amount actually spent. At the end of the year this presents a condensed summary of the family's financial record.

The items in Table XXV do not require any further explanation. The percentage figures in the column marked Monthly Budget indicate the approximate percentages which a family would spend on each of these items if it had an income of $1,800 annually. At least for the first few months some such division of expenditures would provide a fairly accurate start. Then as the family gained experience and kept its own record, changes in the percentages allotted for the various items could be made as well as changes in the items themselves to fit family experience.

TABLE XXV.—SUGGESTED ARRANGEMENT OF ITEMS AND RECORD FORM FOR FAMILY BUDGET

Item No.	Monthly Budget % of Income*	Item	Jan.	Feb.	March	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
1	30	A. Food †	$47											
2	16	Housing												
3	10	Household Operations (fuel, gas, water, electricity, telephone, soap, etc.)												
4	4	Household Furnishings												
5	9	Clothing												
		Father												
		Mother												
		Son												
		Daughter												
6	9	Transportation												
		Automobile												
		Other (bus, trolley, train, etc.)												
7	3	Taxes												
		Income (withholding)												
		Sales												
		Gasoline												
		Property												
		Others												
8	1	Savings												
		Social Security Deduction												
9	2	B. Personal Care												
		Father												
		Mother												
		Son												
		Daughter												
10	3	Medical Care												
11	1.5	Dental Care												
12	4.5 (12–13)	Insurance (life, property, automobile)												
13		Savings												
		U. S. Bonds												
		Tax credits												
		Bank												
14	3	C. Vacation and Recreation												
15	1 (15–16)	Newspapers, Magazines, Postage												
16		Books												
17	3 (17–19)	Dues												
18		Contributions												
19		Gifts												

* The percentages in this column are for an income of $1,800 a year, or $150 a month. In an actual budget, the amounts should be given, instead: $45 instead of 30 %, etc. † Explained on page 324.

Keeping the Records. After drawing up the budget and putting it into operation, the second important step is to keep a record of expenditures. The method of keeping such a record will vary with circumstances and experience. The simplest possible device is needed to overcome inertia and to secure the complete co-operation of all those who spend any part of the family income. In those cases where bills are paid weekly or monthly by check the stub is a convenient record, but cash purchases are usually advantageous, and workers who receive their weekly wages in cash do not as a rule maintain bank accounts. For these reasons a system for recording the daily cash outlays with a minimum of effort is necessary.

How detailed a record should be kept? If expenditures are recorded with considerable detail the record will usually be much more valuable. The classification of food items, for example, serves not only as a record of expenditures for food but also as a means of testing the adequacy of the diet and of comparing the amounts spent on meat, milk, butter, eggs, and cheese to see if the proportions conform to the recommendations of approved family diets. Detailed records may be kept for almost any one of the items and from time to time it may be desirable to keep such detailed records to ascertain the nature of the expenditures and to detect possible leaks. But once this has been done for a period of months for specific items there seems to be no good reason for continuing it. It would probably be the judgment of the average budgeter that the burden of keeping too detailed a record of expenditures outweighs any possible gain.

How accurate should the record be? Let it be said at once that budgeting is not bookkeeping. That being the case an exact balance is unnecessary. The family is not a business unit using the budget to check its monthly program, but is rather a consuming unit using the budget as a guide to better living. The budget and the record of expenditures must always be regarded as a means to an end.

A simple method of recording daily cash expenditures is shown in Table XXVI on page 323. One of these sheets is prepared for each month in the year, and with the budget sheet is kept in a large notebook at a convenient location in the kitchen. A pencil is attached to the notebook and as members of the family come home after a shopping tour or at any other time, they go to the budget book and record all expenditures made during the day.

The column marked "Date" is a device for helping to recall whether a certain expenditure has been recorded. It will be noted that the columns to the left are so small as to allow no room for comment. For the food items the only necessary notations are the date, quantity, and price. The other columns carry items for which some notation is frequently

TABLE XXVI.—SUGGESTED FORM FOR RECORDING DAILY CASH EXPENDITURES

January, 19—

Date	(1) *Food*							*Date*	(3) *Household Operations*	*Date*	(5) *Clothing*
	Butter	Date	Bread	Date	Fruits and Vegetables	Date	Groceries				
	Milk										
	Eggs		Meat						(4) *Household Furnishings*		(6) *Transportation*
										2	$.90 5 gallons gas
	Cheese										
	(2) *Housing*				(15) *Newspapers, etc.*				(7) *Taxes*		(8), (13) *Savings*
								2	$.25 on 5 gallons gas		
	(16) *Books*				(17) *Dues*				(9) *Personal Care*		(10), (11) *Medical, Dental Care*
	(18) *Contributions*				(19) *Gifts*				(12) *Insurance*		(14) *Vacation and Recreation*

desirable. For example, in the transportation account the sample entry shows that on the second of the month ninety cents was spent for five gallons of gasoline, while the tax account shows that a tax of twenty-five cents was paid on the gasoline purchased. Records of this type will be found very helpful in calculating income tax returns.

Checking Expenditures. At the end of the month the figures in each column are totaled and transferred to the proper column on the budget sheet, where a glance at the budget column offers a quick comparison with the amount actually spent in that month. For example, if the amount actually spent in January for food was $47, as shown in Table XXV, it would be $2 over the budget (30% of $150), but January is a long month. The housewife knows that her expenditures for food will run at least that much less than the budget in February so as to maintain a balance. In the same way the monthly expenditure for each item is recorded and compared with the amount budgeted for that item. If overdrafts appear they must be reduced in subsequent months or the budget for that item must be increased, with a corresponding reduction in the budget for some other item. On the other hand, if the comparison reveals several accounts in which the expenditures have been less than the amount budgeted the surplus may be shifted temporarily to some one of the other items. Thus the amount deposited in the savings bank might be increased temporarily. If expenditures for one account consistently fall below the amount budgeted the budget may then be revised so as to allow more for some account which is consistently falling in arrears.

A Family Inventory

Determining Net Worth. At least once each year the family's assets and liabilities should be listed and set forth in equally clear fashion to show what economic progress the family is making. In fact, operating on a budget and recording expenditures is a means not only of revealing the operating expenses of the family but also of showing the net acquisition of permanent wealth. A suggested form of financial statement is shown in Table XXVII. Among the family assets there should be listed the market value of the house (if owned), furniture, and furnishings. On another sheet a much more detailed inventory of the furniture and furnishings is advisable. A copy of this should be kept in a safe place outside the home, such as a safe deposit box, so that in case of fire an accurate listing and valuation of furniture and furnishings can be presented to the insurance adjuster. The resale value of the family automobile will also be included as an asset, as well as the cash surrender value of life insurance policies. That surrender value is stated in the contract or may be secured from the company agent. The accumulation on Social Security

is an asset which will increase year by year, while cash on deposit in the bank is an item which will vary. If the family owns any stocks, bonds, mortgages, or other similar investments their market value should be included in the list of assets.

TABLE XXVII.—SUGGESTED FORM FOR A FAMILY FINANCIAL STATEMENT
January 1, 19—

	Assets	$
1	Market value of house	
2	Market value of furniture and furnishings	
3	Resale value of automobile	
4	Cash surrender value of life insurance policies	
5	Social security accumulation	
6	Cash on deposit	
7	Market value of investments in stocks or bonds	
8	Other assets	
	Total Assets	
	Liabilities	$
1	Mortgage on house	
2	Note held by bank	
3	Borrowed on life insurance	
4	Accounts payable at stores	
5	Other liabilities	
	Total Liabilities	
	Net worth January 1, 19—	

If temporary loans have been negotiated through the bank or life insurance companies, their amounts must be included among liabilities. Likewise accounts payable at stores and any other amount owing should be listed. The difference between total assets and total liabilities represents the net worth of the family at the date of the statement.

A Budget for College Students

One Million Consuming Units. In addition to about 33,000,000 families in our country there are approximately 1,000,000 young men and women in American colleges and universities. While a small number of the college students live at home, most of them live in boarding houses, commons, or fraternities, away from home. While the families represented by these students should include their expenditures in family budgets, it is desirable that each individual student should keep a budget also. Such budgeting serves a number of useful purposes. In the first place it enables the student to give a proper account to his parents of money income received and spent. Budgeting is much more likely to insure the

wise use of funds, the enjoyment of which someone else has forgone. To the extent that a student receives his income in the form of a gift from parents or others he should weigh each proposed expenditure carefully, asking himself whether or not such an expenditure will yield more utility as he proposes to use it than it would have yielded had the donor used it for himself. In many, if not most, colleges the fees which students pay in the form of tuition cover not more than half of the actual cost of rendering the service received. The remainder of the college income is received from endowments and gifts from friends of the institution. This also is a fact which students should keep in mind when contemplating an expenditure of doubtful utility. A third advantage of budgeting on the part of college students is the inculcation of habits of wise and careful consuming. These habits will be valuable aids to the student in his later life. In view of the fact that so many marriages are wrecked on the rocks of financial mismanagement, budgeting by college students is an excellent preparation for successful marriage.

A Sample Budget. Generally speaking, the advantages of budgeting are the same for college students as for families. The technique also is similar. The only difference is to be found in the nature of the accounts. On this page there is a suggested budget form for college students, containing 16 items which in large part cover their specialized expenditures. Such items as tuition, fees, books, board, room, and dues are fairly

TABLE XXVIII.—SUGGESTED BUDGET FORM FOR COLLEGE STUDENTS

	Monthly Budget	*Account*	*Sept.*	*Oct.*	*Nov.*	*Dec.*	*Jan.*	*Feb.*	*Mar.*	*Apr.*	*May*	*June*
1		Tuition										
2		Fees										
3		Books										
4		Board										
5		Room										
6		Clothing										
7		Transportation										
8		Automobile (operating, upkeep, garage rent)										
9		Laundry and cleaning										
10		Medical and dental care										
11		Donations										
12		Dues (fraternity, club, class)										
13		Newspapers, magazines, postage										
14		Recreation (college sports, movies, dances)										
15		Insurance										
16		Taxes (sales, gas, tobacco)										

definitely fixed amounts depending upon the institution. Many colleges also require medical and dental care by the college physician at a flat annual rate. In these days of hitchhiking the item of transportation to and from college may be unimportant. If the student is taken to college in the family automobile the cost involved is properly chargeable to him. Those items in which wide disparities will appear, depending upon the financial resources of the individual, are clothing, laundry and cleaning, donations, and recreation. Many students carry insurance policies whose premiums should be included in the budget. In these days of increasing indirect taxation it is important also for students as for all others to include taxes in the budget. In recording expenditures for gasoline or cigarettes the amount actually paid for the merchandise should be recorded, while the amount superimposed as tax should be separated and recorded under the tax account.

Many students receive supplemental income in the form of scholarships, awards, and wages for various kinds of part-time work. In their income accounts all such forms of income should be included at their money value in addition to the cash allowance received from their parents.

A careful record of expenditures is important and may be kept in the manner already described. After the monthly expenditures have been totaled and transferred to the budget account for comparison, submission of a summary financial statement to one's parents will be evidence that income has been used carefully so as to maximize its utility. Regular receipt of such reports will do more than anything else to assure parents that students are achieving the purpose for which the family is working, which is their own greater welfare.

Summary

Although the form of organization for production has undergone several changes designed to increase efficiency, the family continues as the dominant unit for consuming purposes. Women are the chief buyers, yet as a group have practically no special preparation for their important role. Their task is made especially difficult by the variety of purchases required to operate a household.

Income may be considered as money, goods and services, or as satisfaction realized. Since nearly 80 per cent of American families have inadequate money incomes it is especially important that care be exercised in expenditures. Money incomes may be spent, saved, or given away. In any case budgeting will serve to maximize their utility.

Budgeting is a means of comparing expenditures, promoting rational use of income, balancing irregular income against regular expenditures,

adjusting expenditures to changes in income or size of family, comparing outlays for selected items, detecting and preventing leaks. It is not a means of enlarging money income nor of freeing consumers from the limitations of small incomes. Individual inertia, intangible results, lack of co-operation, and irregular income are common obstacles to budgeting.

The technique of budgeting involves drawing up a budget, keeping a record of expenditures, and checking one against the other. Supplemental to a budget is the family balance sheet which reveals net worth and economic progress of the family. All advantages of budgeting are available to college students, and specific gains repay those who carefully plan and record expenditures.

QUESTIONS FOR DISCUSSION

1. How does your family, as a consuming unit, compare with a corporation, as a producing unit, as to (1) motives? (2) standards of success? (3) qualifications of employees? (4) methods of operation?
2. To what extent is your family a producing unit?
3. Is your family income received regularly or irregularly? Is its expenditure budgeted?
4. Have you ever saved any portion of your income? What were your motives? Why do you think your father saves part of his income?
5. Do you think keeping a budget is worth the effort?
6. Does a business firm operate on a budget? Does it keep a record of expenditures?
7. Do you know the income and net worth of your family? Is such information any of your concern?

PROBLEMS AND PROJECTS

1. Compare the housekeeping activities of your mother with those of your grandmother; list all the economic functions performed by your grandmother, such as baking and canning, and note how many of them have been turned over by your mother to commercial enterprise.

2. Secure from your grandparents information as to their former buying practices; compare them with methods used by your parents. Contrast also the relative influence of advertising on the two generations.

3. Urge your family to draw up and use a budget for 3 months; from the record of expenditures calculate the percentages spent for various items; check these with sample budgets.

4. Draw up a personal budget to cover your college year; keep a record of expenditures and check them with your budget each month; send a monthly financial statement to your parents.

5. Calculate your personal net worth.

6. Review Blodgett, H. A., *Making the Most of Your Income;* or Davis, H. W., *Money Sense;* or Lord, Isabel E., *Budgeting Your Income;* or Harwood, E. C., and Fowle, Helen, *How to Make Your Budget Balance.*

17

Intelligent Buying

Spending the Family Income

Intelligent Buying Increases Real Income. After a family has apportioned its money income among expenditures for food, shelter, clothing, and other items, the next step is to secure maximum quantity and quality when that money is exchanged in the market place for merchandise or services. This requires a knowledge not only of what to buy but also of where and of how to make purchases. Although very few ultimate consumers have such knowledge, it is available. Just as budgeting is the family counterpart of business accounting, so self-development of intelligent buying technique is the counterpart of business purchasing departments. It is the practice among modern large well-managed corporations to maintain a special department whose employees devote their entire time and energy to improving their knowledge and technique in buying the comparatively limited number of materials necessary in a particular business. When these buying experts enter the market the methods they use are altogether different from those which their employers seek to encourage among ultimate consumers. Advertising is used only to the extent that it provides information which will help to reach an intelligent decision. Emotional appeal is ruled out. Specifications are drawn and are submitted to competing producers, who offer to supply desired amounts at stated prices. These wholesale prices usually bear a close relation to costs of production. Contracts are let to the lowest bidders, and as orders are being filled periodical tests of quality are made. If all or any portion of the merchandise delivered fails to meet specifications it is rejected. This method of buying is rational, intelligent, businesslike.

With the above-described method, contrast the buying methods of most ultimate consumers. They are irrational, unintelligent, unbusinesslike. Several reasons for this lack of buying technique have been suggested and examined. The need for adopting wiser consuming standards has been demonstrated by abundant evidence. But wiser consuming standards need to be supplemented by intelligent buying technique if consumers are to realize maximum satisfaction from their incomes. The purpose of this chapter is to describe devices calculated to develop individual effectiveness of buyers. It is not contended that individual

consumers can or should become as proficient as business purchasing agents. The number of things they have to buy, and the limited time they can devote to study and actual buying, preclude all possibility of developing professional skill. What is contended is that by observing a few simple rules and adopting certain practices of proved value ultimate consumers can develop an intelligent buying technique. By sloughing off customary consumer practices, and substituting for them some of the rational methods used by expert business purchasing agents, final consumers may more nearly approach the concept of economic men. In so doing they might exercise that control of production which is supposed to be theirs. The net result would be more goods which consumers want, and goods of better quality at lower prices. Thus progress would be made toward achieving real consumer welfare.

Better buying habits can stretch each consumer's limited number of dollars; can help retail buyers to get their money's worth whether buying necessities, comforts, or luxuries. If one dollar can be stretched so as to secure $1.10 worth of merchandise, or if 90 cents can be stretched to secure a dollar's worth, family real income is increased. This explains why it is possible that of two families receiving identical money incomes one may enjoy much greater real income than the other. The secret is found in wise buying.

From the standpoint of intelligent buying an unfortunate customary view has developed that retail buying is primarily a woman's job. False standards of masculinity and femininity have been carried into this sphere of consumer activity. This custom has grown out of another custom which regards the male as the family head whose sole and sometimes only function is to provide a money income; once that is achieved he has fulfilled his duty. The family division of labor then assigns to the wife and mother the task of converting that money into real income. That task completed, she then has to manage a miniature hotel supplying food and sleeping quarters for the family. In the time that is left she rears her children and engages in countless community projects. It is not surprising that women, being saddled with 50 per cent or more of the retail buying job, have fallen into the easiest, simplest methods. This is the more readily understandable when it is realized that such methods tend to enhance the profits of retail merchants, although the cost of providing telephone service, delivery, and credit may lead to higher prices without resulting in greater profits. The first step, then, in developing an intelligent buying program, is for husband and wife to work together in sharing the responsibilities of buying. In many cases this means that men will have to assume a greater responsibility. Just as family budgeting can succeed only when the two family heads co-operate,

so development of buying technique can be achieved better when they plan and make their purchases jointly.

Developing the Art of Buymanship

Buymanship Versus Salesmanship. In discussing advertising and salesmanship it was shown that an effort has been made to put selling on a scientific basis. The technique is to break down sales resistance. The objective is to expand profits. Better buymanship seeks to substitute rational for emotional guides in buying. The objective is to increase consumer satisfaction and welfare. Better buymen develop greater resistance to customary selling methods. Properly regarded, there is no sales resistance. Consumers need and want goods to satisfy their desires. In that sense there is no need for developing sales resistance. What is needed is resistance to methods based on emotional appeal. Consumers need not only goods and services; they need to get, for their money, the most they can in amount and quality. Buying and selling are but two phases of the same process. They are complementary rather than opposing actions. Whereas scientific selling emphasizes opposition between seller and buyer, better buymanship seeks to promote co-operation between buyer and seller. Better buymanship will not reduce the profits of legitimate retail merchants, while it will increase utility for final consumers.

The first step in developing better buymanship is to fortify oneself with specific technical information at home before going to market. Just as the professional purchasing agent proceeds to study the products he needs and to draw up specifications of quality, so the ultimate consumer needs to study the products he needs and to acquire some knowledge of devices for measuring or ascertaining quality characteristics. Armed with such information, the retail buyer is provided with comparative knowledge which enables him to ask intelligently for specific information. Since price without reference to quality is meaningless, it is important for the potential buyer to be supplied beforehand with price *and* quality information. Considerable evidence has been presented to show the helplessness of modern individual consumers in attempting to get this information for themselves. There are, however, a number of sources to which they may turn for specific technical information concerning quality and price of merchandise available in the open market. From among these sources the following seven are described and evaluated briefly.

Sources of Technical Information: (1) *Consumers' Research, Incorporated,* Washington, New Jersey. In 1927 a book by Stuart Chase and F. J. Schlink, describing the plight of consumers in attempting to get their money's worth, caught popular fancy and became a best seller. Growing

consumer consciousness of the need for help was rendered articulate by lively revelations of quackery, fraud, misrepresentation, and disparity between quality, prices, and cost of production. The latter part of the book was devoted to consideration of agencies for assisting consumers. By the very nature of things this discussion was general rather than specific. After reading the book many consumers wrote to the authors asking how or where they could get specific technical information to serve as a guide when buying merchandise. These expressions of widespread consumer interest resulted in the formation of a nonprofit corporation to serve as a research agency and clearing house for consumer information. On the basis of tests made in their own laboratories, supplemented by information from other sources considered to be reliable, Consumers' Research issues *Bulletins* in which widely used products are listed by name as recommended, intermediate, or not recommended. Information is given also as to whether standard prices are low or high. Thus consumers are informed that although some articles are recommended as being of good quality, they are overpriced. From a small, comparatively local group, Consumers' Research has grown to a national organization whose main offices and laboratories are now located at Washington, New Jersey. This growth is remarkable for two reasons. Unlike commercial organizations, Consumers' Research has used no aggressive, promotional activities. There are no paid sales representatives seeking subscribers. Advertising has been largely by word of mouth. The second remarkable feature is that consumers pay a subscription fee. The general *Bulletin* for which anyone may subscribe at the rate of $3 a year combines specific technical reports with general consumer news and information. The *Annual Cumulative Bulletin* is published as a condensed buying guide, and costs $1. Considering the potential savings made possible by the use of this service, the $4 fee for the two publications might be regarded as nominal. But the fact that so many thousands of consumers are willing to pay it is an indication of their growing desire to become better buyers.

In a profit economy motives are always suspect. Questions are raised concerning the reliability and the integrity of Consumers' Research. No matter what else one may think about the organization, its integrity has never been questioned successfully. The suggestion that large corporations pay fixed fees for recommended ratings loses plausibility if one examines the *Bulletins* over a period of time. The products of a particular corporation may be highly rated in one *Bulletin* and not recommended in another, or one product may be recommended while in the same *Bulletin* another product of the same company may be given a low rating.

Although one may accept Consumers' Research *Bulletins* as reliable

there are very definite limitations to the service. Since income is secured from subscription fees and receipts from sales of publications, its financial resources are limited. Compared with the advertising appropriation of any sizable corporation the amount spent by Consumers' Research to inform its subscribers is small indeed. Measured in terms of comparative value received, subscribers get more than their money's worth, but measured in absolute amounts the limited resources of Consumers' Research restrict seriously the scope of its operations.

Because of libel laws, much information must be presented confidentially. This operates to restrict growth in the number of subscribers. While commercial advertisers may make exaggerated claims, Consumers' Research is restricted to statements of fact which can be proved in a court of law. Anyone familiar with legal procedure knows that an economic fact is not necessarily a legal fact.

Combined with financial limitations, the vast expanse of the United States operates as an obstacle. In discussing custom it was shown that consumer practices vary geographically. Also branded products available in one section are not available in another. A basic limitation to Consumers' Research is its complete dependence on the structure of established trade-marks and brands. In many cases unmarked and unbranded merchandise might be superior or acceptable but there is no way of discovering or providing such information.

Regarded in its broader aspects as a social force, Consumers' Research is subject to limitations not all of which are necessary. A serious limitation arises out of the attitude which those in charge of Consumers' Research have taken toward social questions. It is their contention that no effective account can be taken of such questions as wages, hours, and working conditions of those engaged in producing the merchandise on which reports are made. Intelligent consumers do not wish to purchase high quality at low price if low prices have been secured at the expense of unorganized workers. If in addition to information on quality and price, subscribers were given a general statement as to the labor policy of the manufacturer or the distributor, or both, they would then have an additional necessary basis on which to make a wise choice. It cannot be argued successfully that such information is unavailable. In fact, on at least one occasion such a general statement was presented in connection with a report on hosiery. Subscribers were told that although hose available at a particular chain store were of good quality and low in price the conditions under which they were made were probably the worst in the industry.

The organization and control of Consumers' Research result in a second limitation to its greater effectiveness. Although organized as a

nonprofit corporation devoted to consumer interests it is controlled by a small self-perpetuating group who are thus self-entrusted with full power to determine policy. Subscribers have no more control than have subscribers to a popular magazine such as *Good Housekeeping*, which also purports to operate a service for the benefit of consumers. While urging consumers to organize to protect their rights, those in charge of Consumers' Research resented the activities and actions of employees in organizing to protect their economic interests as workers. This led to a strike in September, 1935. Technically those in charge of Consumers' Research won the strike, but in doing so alienated a number of subscribers who were concerned with something more than mere quality and price information. Some of these were active in founding a new organization which now operates as a second source of technical information for consumers.

(2) *Consumers Union of United States*, 17 Union Square, W., New York City, was chartered in February, 1936, "To furnish unbiased, usable information to help families meet their buying problems, get their money's worth in their purchases, develop and maintain an understanding of the forces affecting their interests as consumers." As might be expected, considering the origin of this new organization, there are several points of similarity between its methods and those of Consumers' Research. The main objective is to provide a technical buying guide for subscriber members. This is accomplished by publishing a monthly *Report* which contains results of laboratory tests, controlled tests under conditions of use, or the experience of a large number of persons. These *Reports* are published in more attractive form than those of Consumers' Research and distinguish for subscribers among "best buys," those "also acceptable," and those "not acceptable." This service is provided at the rate of $3.00 a year. Like the *Bulletins* of Consumers' Research, *Consumer Reports* contain much useful information. In addition to general articles, each report on specific merchandise is prefaced with a statement of what consumers should know when they set out to buy a particular brand. Thus a report on stockings is supplemented by a semitechnical statement telling consumers how to judge quality of hose. Likewise, reports on soaps and toothbrushes are rendered more valuable by supplementary statements telling consumers what they need to know in choosing among many brands. The *Buying Guide* is issued in December. In convenient pocket size its 380 pages condense information in the preceding issues and include new material and special buying advice. In 1940 Consumers Union started a weekly publication called *Bread & Butter*, which reports every week on new and predicted price and quality changes in consumer goods, interprets legislation as it affects consumers,

reports on government regulations affecting consumers, and gives timely advice on the purchase and preparation of food. These three publications are available for a subscription fee of $4 annually.

Consumers Union, like Consumers' Research, is faced with the problem of convincing subscribers of its reliability and integrity. In general, comments made concerning Consumers' Research may be applied to Consumers Union. Evidences of reliability include a financial statement certified by public accountants, and a knowledge of the personal integrity of those officially connected with the organization. The officers and directors are persons of recognized achievement in their individual fields. More than seventy educators, social workers, and scientists sponsor Consumers Union, and a national advisory committee of forty-nine consumer leaders contributes to the formulation of policy. There are, moreover, cases in which one product of a corporation will be given a high rating, while another is labeled as not acceptable. Additional evidence is the fact that a product may receive a high rating while a supplementary statement concerning the labor policy of the company is sharply critical. An added safeguard is the fact that each subscriber is a member of the organization, entitled to one vote in electing officials who determine its policy. It is too early to judge whether this device actually will result in democratic control, but at least, and unlike Consumers' Research, machinery for such control is provided. Thus far, the number of Consumers Union members participating in the annual nominations and election of officers and directors has represented 25 per cent or more of the total membership. In comparison with commercial corporations and even with consumer co-operatives this is high.

This leads to a further discussion of differences between the two organizations. Consumers Union, unlike Consumers' Research, is concerned with wages, hours, and working conditions of employees in factories making merchandise on which reports are published. While the problem of securing information is difficult, it is not insurmountable. Reports on automobiles and mechanical refrigerators are supplemented by reports on conditions of labor in the plants making them. Thus members are informed of the antiunion policy of one automobile manufacturing company and are told that independent unionism is strong in another. Moreover, one issue contains a list of goods whose makers are reported as unfair to labor. All members of Consumers Union staff not affiliated with the management belong to the Book and Magazine Union which is affiliated with the United Office and Professional Workers of America, C. I. O. In contrast with the wide disparity between wages of employees and salaries of officials reported as characteristic of Con-

sumers' Research, the minimum wage (as reported in 1944) is $23 a week while the maximum is $100.

A second difference between the two organizations is reflected in the willingness of the newer group to co-operate with other organizations interested in consumer welfare. Consumers Union joins hands with consumers' co-operatives, with other consumer clubs, and with trade unions. In line with this policy Consumers Union is willing to provide technical assistance to consumers' co-operatives by testing and rating their products.

Allusion has been made to a third fundamental difference between the two organizations. Whereas Consumers' Research subscribers have no voice in electing officials or controlling policies, subscribers to Consumers Union are by virtue of that fact members of the corporation entitled to one vote each. This is patterned after the consumer co-operative device for achieving democratic control. If members wish to change officers or policy they have opportunity to express their convictions by ballot. This is altogether harmonious with the general aims and purposes of such an organization.

Except for organization and control and attitude on labor policy, limitations to the effectiveness of Consumers Union are identical with those discussed in connection with Consumers' Research.

In conclusion it may be said concerning both organizations that the nominal membership fee may be returned many times over in savings resulting from purchasing intelligently. On a single purchase of expensive articles such as automobiles or mechanical refrigerators members may save enough to pay their subscription rate for several years. On smaller items purchased more frequently, such as soaps, hosiery, toothbrushes, gasoline, or motor oils, cumulative savings resulting from following suggestions of technical experts will amount to surprisingly large sums. Similar though they are, the two organizations are yet so distinctive as to justify fully the use of either one or both services.

Consumers are sometimes puzzled by the fact that Consumers Union and Consumers' Research do not agree fully on their recommendations. Yet this is not surprising. In fact, it would be more surprising if they did agree. The intelligent user of these services will use their recommendations as guides, not as mandates. Even if he does not follow the recommendations of either agency, he will have learned enough in reading their reports to enable him to make a more intelligent purchase.

Similar to these two agencies in its general organization and operation is Intermountain Consumers' Service, located at Denver, Colorado. Geographical differences in customs, brands, and prices enable this agency to serve its subscribers in the Mountain and Pacific Coast states.

In his *Folly of Instalment Buying*, Roger Babson expresses his approval of associations of consumers to meet organized exploitation with organized protection. His criticism of the ones in existence are that they have failed "to attack the excesses of instalment buying as violently as they should." He expresses the hope that consumers' organizations will be able to strengthen their position in Washington so that lobbies of other interests will be offset by consumer lobbies.[1]

(3) *Government Publications.* Sources of consumer information published by the Federal government are of two types: (*a*) *Consumers' Guide* and (*b*) various departmental bulletins. *Consumers' Guide* in 1943 was being published monthly by the War Food Administration, United States Department of Agriculture. This was going without charge to 140,000 whose names were on the mailing list. Additional copies may be obtained from the Superintendent of Documents, Government Printing Office, Washington, D. C., at five cents a copy or fifty cents a year. Starting as a bi-weekly publication, *Consumers' Guide* dates from September, 1933. It was then published by the Consumers' Counsel Division of the Agricultural Adjustment Administration. When the recovery acts for agriculture and industry were inaugurated it was realized by administrative officials that prices for practically all consumer goods would rise. Efforts were made, however, to give consumers factual information, and an attempt was made to render unnecessary price increases impossible. To that end, in the Agricultural Adjustment Administration there was organized a division known as Consumers' Counsel. The original and primary purpose of Consumers' Counsel Division was to prevent unnecessary pyramiding of prices in what was expected to be a temporary period of readjustment. This was to be accomplished by supplying consumers with price information based on average prices of important commodities in fifty-one cities, and published in the *Consumers' Guide.* The editors of *Consumers' Guide* believed that consumption is the end and purpose of production:

> "To that end the *Consumers' Guide* emphasizes the consumer's right to full and correct information on prices, quality of commodities, and on costs and efficiency of distribution. It aims to aid consumers in making wise and economical purchases by reporting changes in prices and costs of food and farm commodities. It relates these changes to developments in the agricultural and general programs of national recovery. It reports on cooperative efforts which are being made by individuals and groups of consumers to obtain the greatest possible value for their expenditures."

[1] Babson, Roger, *The Folly of Instalment Buying*, pp. 120, 121, J. B. Lippincott Company, Philadelphia, 1938. For further evaluation of these agencies see Bush, George L., *Science Education and Consumer Buying*, *op. cit.*, chap. 4.

For several months *Consumers' Guide* was scarcely more than a price-reporting service published in mimeographed form. In the spring of 1934 a series of special articles was begun. Since that time special articles have become a permanent and important feature. Through various issues consumers have been informed concerning milk, ice cream, sugar, potatoes, oranges, apples, strawberries, tomatoes, bread, and numerous other food products. In other special articles women buyers have been presented with year-round buying calendars for meat, fruits, and vegetables. By following information presented in these articles women may become better buyers by adjusting their purchasing habits to well-defined seasonal variations. A similar service is that which informs consumers which food products are likely to be abundant and which may be scarce. On the basis of such information buyers may either lay in a stock or may alter their buying habits to include cheaper yet satisfactory foods. Several articles have appeared concerning the co-operative movement, while others have emphasized the need for standards, particularly for canned goods.

Following is a partial list of articles which have appeared in *Consumers' Guide* in recent years. Files of *Consumers' Guide* are doubtless available in many libraries and Consumer Information Centers. It is quite likely also that many of these can be secured as reprints. The figures at the right show the date of the issue in which the article appeared (for example, 12-2-40 means December 2, 1940).

What Grade of Eggs Do you Buy?	12-2-40
Milk Glossary for Consumers	12-2-40
Bread Facts for Consumers	12-16-40
Your Food Supplies and Costs	12-16-40
A Citrus Saga	1-15-41
Facts about "Enriched" Flour and Bread	2-15-41
Stretching Your Cotton Goods Budget	2-15-41
So You're Buying an Iron?	3-1-41
Consumers Services of the Department of Agriculture	3-1-41
Standards for Consumers	3-15-41
Buy Shoes That Fit	4-1-41
New Labels for Woolen Goods	5-1-41
Credit Unions Help You Save	8-41
Mildew Can Be Prevented	11-1-41
More Heat, Less Fuel	12-15-41
Tips on Stretching the Life of Household Goods	1-15-42
Squeezing the Water Out of Food	2-1-42
Fat of the Land	2-15-42
What's in the Price Control Law	4-1-42
Sheets and Pillowcases Get a Label	4-1-42

Is Your Medicine Chest Ready for Emergencies? . .	9-42
So You're Buying a Fur Coat	11-42
School Lunches Must Go On	2-43
Make the Most of Meat	3-43
Shopping Is a War Job Now	6-43
Pack That Food Away	7-43

The influence of the period during which the United States was preparing for war is clearly indicated in the titles during 1940 and 1941. Beginning with the 1942 issues the influence of the war is evident, the articles dealing with conservation, preservation of food, price control, and rationing.

Information presented in *Consumers' Guide* is general rather than specific. It is, in fact, primarily a means of consumer education rather than a buying guide. Unlike any of the sources of information so far described no attempt is made to present information concerning specific brands. If the pages of this publication were used to present consumers with specific information taken from files of the National Bureau of Standards it might quickly and easily become the outstanding buyers' guide in the country. There is little likelihood that this will ever be done, however, because opposition of manufacturing interests will prevent it. In fact, these very interests have even opposed the dissemination of general information to consumers. First they curtailed and then during the war period succeeded in eliminating Consumers' Counsel Division. The law establishing the National Bureau of Standards makes no provision for the publication of its findings, and this vast storehouse of information will never be available to consumers until they secure a change in the law. Nevertheless *Consumers' Guide* represents a significant venture by the Federal government. Heretofore governmental facilities have been used freely to assist producers, but they have been used to a very limited extent to benefit consumers. For the present consumers anxious to develop themselves as better buyers will do well to place their names on the mailing list to receive *Consumers' Guide.*

Although there is no single department of the Federal government devoted to consumers' interests, departmental bulletins are published by various bureaus, particularly in the Departments of Agriculture, Labor, and Commerce, which are engaged in the task of collecting and disseminating information which is useful to consumers. Price list 76, entitled *Government Publications of Use to Consumers*, is available without cost from the Superintendent of Documents. This 18-page pamphlet presents in well-indexed form all the publications issued by various departments which are of interest to consumers. The more important classifications include bulletins dealing with food, clothing, cost of living,

consumers' co-operation, house, home, and garden. Every individual, or every group of consumers interested in developing themselves as good buyers, should have a copy of this bulletin.

Present Guides for Household Buying is a 25-page pamphlet issued by the United States Department of Agriculture as Miscellaneous Publication No. 193. It may be secured from the Superintendent of Documents for five cents. In concise, practical, useful form the author of this bulletin describes existing types of consumer guides and quality grades now in use in marketing food, clothing, household equipment, and several miscellaneous commodities.

A Fruit and Vegetable Buying Guide for Consumers is a 60-page bulletin issued by the United States Department of Agriculture as Miscellaneous Publication No. 167, priced at five cents. This bulletin contains useful hints on how to buy fruit and vegetables wisely. The more commonly used fruits and vegetables are arranged alphabetically, each one being discussed individually. This bulletin together with the two above described should be found in every kitchen library.

Typical of some of the more specialized information available are leaflets 103, 105, and 117, describing quality guides in purchasing sheets and pillow cases, women's ready-made dresses, and women's cloth coats. These 8-page leaflets may be obtained for five cents each. In a few minutes preceding a shopping tour an intelligent consumer can glean from these pages information which will prove helpful when she enters the market place.

A special mimeographed article issued by the Department of Agriculture entitled *The Consumer and the Standardization of Farm Products* is designed to acquaint retail buyers with quality standards which may be used as buying guides in purchasing such agricultural products as meat, poultry, butter, cheese, and eggs.

A particularly helpful collection of information is contained in *Simple Consumer Tests* issued as Supplement No. 1 to Bulletin 3 of the Consumers' Counsel Division. This 7-page, mimeographed bulletin describes simple tests which may be used in the home for judging fiber content of textiles, possible shrinkage of washable fabrics, fastness of color, and durability of silk hose. For example, consumers are told that in purchasing silk hose the top of the stocking should stretch to eleven or twelve inches. Failure of a stocking so to stretch is an indication that economy has been sought by using less silk, which means that the stocking will not last as long. The stretch from heel to instep should be seven inches. Other simple tests are described for detecting excess water in household paint, for testing the stainless quality of steel, and the lubricating quality of household oil.

There has been a steady flow of valuable bulletins for consumers since 1941. *Vitamin Values of Food in Terms of Common Measures*, Miscellaneous Publication No. 505, and *The Road to Good Nutrition*, Children's Bureau Publication No. 270, contain useful general information. *Milk for the Family; Home Canning of Fruits, Vegetables and Meats; Homemade Bread, Cake and Pastry; Homemade Jellies, Jams and Preserves;* and *Meat for Thrifty Meals*, may be secured from the Superintendent of Documents, for five or ten cents each, by asking for *Farmers' Bulletin* Nos. 1705, 1762, 1775, 1800, 1908.

Before going to market, a consumer buyer would do well to consult *Guides for Buying Sheets, Blankets, Bath Towels; Fabrics and Designs for Children's Clothes; Judging Fabric Quality; Cotton Shirts for Men and Boys;* and *Buying Boys Suits*. These, too, may be secured from the Superintendent of Documents by ordering *Farmers' Bulletin* Nos. 1765, 1778, 1831, 1837, 1877. A series of mimeographed bulletins issued by the Consumer Division of the Office of Price Administration is available at various Consumer Information Centers at no charge. The series runs under the title *Wise Buying in Wartime* and includes such food items as beef, tomatoes, eggs, and many others.

(4) *Better Buymanship* Bulletins, published by the Household Finance Corporation, 919 North Michigan Avenue, Chicago. The Household Finance Corporation is one of the larger personal-loan companies operating in the United States. As a part of its services to borrowers, and probably as an indirect means of increasing the possibility of repayment of loans, a department of research has been created which has published 27 pamphlets under the general title of *Better Buymanship*. Recommendation of these pamphlets is not to be construed as approval of the business policies or practices of the company. Judged entirely on their merits, the bulletins are sources of helpful information, and for that reason, and that alone, are recommended. They give helpful, concise, and specific information to prospective buyers of practically everything required in a household, from food, clothing, and household equipment to gasoline, tires, and cosmetics. They are well written, authoritative, and well organized. At the back of each one is a green sheet containing points to remember when buying the articles discussed in that pamphlet. Buyers are urged to tear this page out and carry it with them on shopping tours.

The sort of information contained in the *Better Buymanship* pamphlets is much more like that to be found in *Consumers' Guide* and in special governmental bulletins, than like that supplied by Consumers' Research or Consumers Union. Their convenient form and arrangement, together with the excellent material they contain, fully qualifies them for a place

in the kitchen library. They are available at the nominal rate of two for five cents.

In addition to these specific pamphlets, the Household Finance Corporation has published a useful bulletin called *Money Management for Households* and another entitled *Stretching the Food Dollar*. The first of these deals with the technique of budgeting, while the second presents suggested diets and general hints on how to buy economically. These should prove particularly helpful to young, inexperienced housewives.

(5) *Journal of Home Economics*. The American Home Economics Association, 620 Mills Building, Washington, D. C., is an organization that works closely with the Bureau of Home Economics of the United States Department of Agriculture. It publishes the monthly *Journal of Home Economics*, containing articles of general interest to consumers and Consumer Education Service. The Association seeks to promote consumer welfare also by representing consumer interests before educational groups and supporting or opposing proposed legislation. Reprints of articles of special interest to consumers are available, as are *Consumer Purchasing Leaflets* prepared by the Committee on Standardization of Consumers' Goods. These include suggestions on how to buy sheets, blankets, and refrigerators.

(6) *Books*. In recent years many books have been written for consumers. Some of these are particularly useful reference books to consult before going to market. The Council on Food of the American Medical Association has published *Accepted Foods*, a book which lists branded food products which have been tested and approved by the Council. Adelle Davis's *Vitality Through Planned Nutrition*, and *Eat Well for Less Money*, by Gaynor Maddox, contain helpful suggestions. *Food Buying and Our Markets*, by Monroe, Kyrk, and Stone, and Margaret Reid's *Food for People*, contain chapters which will help the general buyer.

Outside the realm of food buying there is a variety of books. *How to Spend Money*, by Ruth Brindze, is still a valuable guide for reference. Her later *How to Stretch Your Dollar in Wartime* is a timely pre-shopping guide. *More for Your Money*, by H. Bennett, contains specific information on buying cosmetics, drugs, certain foods, wines, liquors, soaps, cleaners, and so on through a list of twenty-seven items. *Consumer Goods*, by Edward Reich and Carlton Siegler, is an excellent and dependable source of general information on textiles, furs, leather, wood, paper, rubber, glass, china, metal, stone, oil, paint, and cosmetics. A final suggestion is that of William Weiss, *How to Keep Out of Trouble*, of which chapters 1, 2, 3, 4, 14, 27, 28, and 30 are particularly applicable.

(7) *Advertising*. If one looks to modern advertising for extensive and reliable factual information he is doomed to disappointment. The con-

sumer who is attempting to develop qualities of buymanship must rely on sources of information previously described in this chapter. There is, however, a type of information which the wise buyer will be able to secure from advertisements. This is price information, to be found almost exclusively in newspaper announcements. It is common practice among food stores to feature special prices on certain articles over the week end. Other stores, particularly department stores, feature prices of a wide variety of merchandise from day to day, climaxed by special announcements for special sales. The wise buyer, fortified with factual information making possible some comparison of quality, will save many steps and considerable time by comparing the newspaper advertisements of competing merchants. It will be found frequently that identical trademarked or branded merchandise will be offered at a lower price in one store than in another. It is much easier to discover this by reading advertisements than by trudging from store to store.

By comparing prices in mail-order catalogues and wholesale catalogues, if they are available, the careful buyer is able to judge somewhat better whether prices asked are fair or too high. Armed with quality and price information, the prospective buyer then enters the market, having done the best he can to qualify as an economic man.

Planning Purchases Versus Hand-to-Mouth Buying. When the consumer is armed with the technical information gleaned from the various sources described in this chapter, the next step in developing the art of buymanship is to plan purchases in advance. Nothing is more helpful in swelling the profits of retail merchants than the practice of many buyers of purchasing in small quantities only when the need is imperative. The housewife who cannot complete a meal without running to the store must first learn to plan her purchases if she wishes to stretch her dollar. On recurring items, of which food is probably the most important, family needs should be planned a week or so in advance and purchases made in large quantities once or twice a week.

Higher prices for smaller quantities do not mean that retail merchants are making proportionately larger profits. To handle a small purchase requires as much labor for bookkeeping, wrapping, and delivery as in the case of a much larger amount. According to value theory this extra cost must in the long run be added to the price. It is an unnecessary cost, however, and one which can be eliminated. Consumers can save large percentages on their purchases if they buy in bulk or large containers.

It is necessary, of course, to purchase some articles in packaged form. Where this is true the wise consumer will buy the largest package, considering the requirements of her family. In one survey, for example, it was found that salad dressing in 3-ounce jars cost 135 per cent more per

quart than if purchased by the gallon, and 121 per cent more per quart than if purchased by the quart. Salt in the package cost 233 per cent more than bulk salt in a 25-pound sack.[1]

Further evidence of economies resulting from large rather than small purchases is found in a study made in Washington. By purchasing 50-ounce jars of tomato juice instead of a 12½-ounce size a saving of 38 per cent could be effected; 36 per cent could be saved by purchasing 31-ounce cans of cherries rather than the 11½-ounce size. In buying lima beans one could save 37 per cent by taking the 20-ounce instead of the 11-ounce cans. Cocoa in 3-ounce containers cost 33 per cent more than in pound packages. Of these and other items included in the survey, savings of 30 to 38 per cent could be made by purchasing eleven items in the large rather than in small packages; savings of 20 to 30 per cent could be made on six items, and of 10 to 20 per cent on twelve items; the minimum saving was 8 per cent in purchasing tea in the 8-ounce rather than in the 4-ounce package.[2]

Custom, fortified by modern advertising, has developed many food fads which are detrimental to family economy. All necessary roughage may be secured by eating fresh foods and vegetables without resorting to special preparations. Raisins do contain iron, but weight by weight they contain less than fresh spinach or meat. While it is true that milk is the best all-round food, even it does not provide all the needed essentials. White-shelled eggs command a higher price than brown ones in New York, while brown ones are sold at a premium in Boston, although their food value is identical.

Further economies can be realized by following a plan such as that suggested in *A Fruit and Vegetable Buying Guide for Consumers* (page 340). Slavish devotion to certain foods, resulting in their purchase when the supply is limited and price is therefore high, causes unnecessary expense. By following a plan for purchasing fruits and vegetables in season, significant savings can be made. This applies also to such unusual situations as scarcity of certain food products caused by drought. Reference to a particular issue of *Consumers' Guide* will inform consumers which food products are abundant and which are scarce, and to what extent variations in price may be expected. The wise buyer then plans her purchases so as to include the more abundant, lower-priced products.

In one respect urban dwellers of today are able better to plan purchases because they have modern mechanical refrigeration facilities for

[1] THOMAS, Elizabeth, *A Comparison of Prices for Bulk and Packaged Goods*, an unpublished manuscript on file in the Department of Economics, Denison University.

[2] *Consumers' Guide*, May 20, 1935 and HAMBIDGE, Gove, *Your Meals and Your Money* p. 117.

preserving food. On the other hand, they are frequently handicapped by their lack of suitable storage space for such commodities as apples, potatoes, and other bulky products.

A very real obstacle to planned purchasing may be limited incomes. In order to secure the best bargains buyers must not only plan to buy at the right time, but must be able also to pay cash. Many times consumers can gain much more than the interest which savings banks pay on deposits by investing the same sums in staple commodities at low prices. But if one's income is uncertain or is too small for a proper standard of living, obviously it is often impossible to purchase for cash in large quantities. For those, however, who do have the cash and the necessary storage place there is no excuse for failure to secure large savings by spending wisely.

Timing Purchases. On larger and more durable items wise consumers refuse to follow the crowd. Most buyers make no plan for future spending. They are less provident than squirrels or bees. Knowing that they will want new spring clothing for Easter wear they wait until the Saturday afternoon before Easter to make their purchases. No coal is laid in until the first cold snap appears, while furs are purchased at the peak of demand in the fall, and furniture in the midst of a holiday season.

Wise buyers reverse this process by purchasing their coal in April, saving as much as 20 per cent. Clothing is bought not when it is needed, but when good bargains are available. A wise buyer will purchase several dresses or suits at a good sale price even though they may not be needed for some time. Furs and furniture will be purchased in August sales, while Christmas gifts will be secured far in advance. Indeed in the case of certain small, easily stored articles some buyers secure their Christmas supply almost a year in advance, during the January sales. Again it is necessary not only to plan ahead, but to have some cash reserve in order to carry out such a buying program.

The wise buyer recognizes also that food prices vary seasonally. Egg prices vary by as much as 100 per cent, potatoes by 60 per cent, onions by 55 per cent, and cabbage by 70 per cent. Five cents invested in *A Fruit and Vegetable Buying Guide for Consumers* will, if its contents are followed, yield several hundred per cent return in savings.

Bargain for Better Prices. If one is to develop the art of buymanship it is important to remember that the so-called one-price system is not ironclad. One should become a careful, cautious, hesitant purchaser rather than an eager buyer. The latter type not only fails to secure any discount in price, but often, by his very eagerness, leads a merchant to boost his price. There are several ways in which price reductions may be secured. First and most direct is an outright reduction in list price.

This is not as difficult to secure as most buyers believe. By using exactly the same competitive weapons that businessmen use when they set out to make purchases, price concessions may be secured. Normally the buyer need have no compunction in using such tactics, for the seller will not cut his price to a point too low to cover his cost.

Price reductions may be secured indirectly by bargaining for a larger allowance where a used article is being traded. In selling such things as typewriters, vacuum cleaners, refrigerators, and automobiles, dealers allow a considerable margin for trade-in allowance. For the careless buyer only a part of this allowance will be made, while the shrewd buyer will bargain till he secures the full amount.

Another way of securing an indirect price reduction is to prevail on the seller to include certain extra items or services not usually included in the list price. For example, the buyer of an automobile may secure some extra equipment, while the purchaser of a household appliance may secure free installation.

A shrewd buyer will attempt to secure an open discount from the retail price. The extent to which retail prices are marked up over wholesale prices has been studied. In many cases it is quite possible to secure through employer, professional, family, or friendly connection a discount ranging from 10 to 40 per cent. A large business firm or educational institution buys all needed supplies at wholesale prices. Frequently it is possible to extend the privilege of wholesale buying to employees affiliated with the firm or institution. All employees of a certain electrical company, for example, may purchase electrical supplies at a discount of 35 per cent, while the 1,500 faculty members of a certain large university may purchase through that institution's purchasing department any article at the same wholesale rate as that paid for the article by the university. Department stores commonly give a discount to employees. It is often possible for a group of buyers to band together to form an association which may make arrangements with local dealers for wholesale purchasing. A common practice for merchants is to sell to such groups at the wholesale price plus 10 per cent, which is a reasonable allowance for the retail merchant's service. In Philadelphia there is an Association of United Fraternal Buyers through which consumers may purchase a wide range of standard products, especially household requirements, at a uniform discount of 20 per cent. Membership in the Association is free, its organizers receiving their reimbursement through an arrangement with co-operating stores. Thus an unaffiliated buyer purchasing a $100 item will pay the full purchase price, while an affiliated member can secure it for $80.

According to merchandising sources the practice of "buying it at

wholesale" has reached "alarming proportions." In 1939 the National Retail Furniture Association started a campaign to stop the rapid growth of "wholesale" buying. A survey in Boston indicated that 71 per cent of the electric roasters, 50 per cent of the food mixers, 33 per cent of the automobile tires, and 21 per cent of the mechanical refrigerators purchased by consumers were secured at a discount. Furniture dealers estimated that 15 per cent of all furniture purchases were made outside the regular retail market, at a loss to retailers of $150,000,000 a year. Using that figure as a base, one of the Association officials estimated that all American retail merchants were losing at the rate of $1,000,000,000 annually as a result of what they described as trade diversion. The largest single channel of trade diversion was reported to be the practice of corporations making purchases for employees and friends of employees. Determined to forestall any further trade diversion the National Retail Furniture Association spent $100,000 in four years. The campaign has taken three different forms. Through publicity consumers have been warned that they are more likely than not to be gypped when they think they are purchasing at wholesale. The second line of action has been to get employers to promise not to sell to their employees any product not manufactured or handled by the firm. The third line of defense has been to get state legislatures quietly to enact a so-called trade diversion bill.[1] As passed in May, 1943, in the state of Ohio, the act forbids any firm engaged in any enterprise in that state to sell or to procure for sale to its employees any article or merchandise not of its own production or not handled in its regular course of trade; but there are a few exceptions such as confections, meals, and tobacco products. Violation of the law is a misdemeanor punishable by a fine of $100 for the first offense and $300 for each subsequent violation.[2]

Shop Around. The buyer who never shops around is simply subsidizing the few firms with which he deals. Considerable evidence has been presented which demonstrates forcibly that prices for identical products are much lower in some stores than in others. The wise buyer will compare quality and price at several stores. In fact, in the case of some items quality and price in different markets must be compared. In the Granville study it was discovered that prices for identical products

[1] By 1943 such laws were on the statute books of Illinois, Michigan, Minnesota, Ohio, Pennsylvania, Wisconsin.

[2] For further information concerning this topic see GARNISS, Arthur L., *Trade Diversion; Consumer Deception through Trade Diversion; Studies and Reports on Industrial Selling*, New York Council on Retail Trade Diversion, 60 East 42nd Street, New York, 17; also *Business Week*, August 19, 1939; and *New York Times*, May 14, 1942; *Printer's Ink*, "*Black Market in Peacetime*," August 6, 1943; *Printer's Ink*, September 3, 1943; *New York Times*, September 10, 1943.

in chain stores were lower in Newark, seven miles away. It was discovered further that on certain items prices in the Newark farmers' market were still lower. Frequently these comparisons in price may be made by following newspaper announcements. This is especially true in the case of larger articles where the prospective buyer is relying on an organization such as Consumers' Research or Consumers Union for recommendations as to quality.

In the process of shopping around it is important to make intelligent use of salespersons. The key word in the preceding sentence is *intelligent*. The careful buyer will find all too frequently that a salesperson is not competent to answer legitimate questions. A quick survey made in a number of states revealed that either no information or insufficient information was obtainable from the labels or from the salespersons as to the breaking strength of the fabric in men's shirts, for example. Other questions to which there were no satisfactory answers related to the presence of sizing in materials, the effect of perspiration on the permanency of color, the effect of washing on color permanency, and the effect of perspiration on women's hosiery.[1] On the other hand, there are shopping centers where capable salespersons are in attendance and full use should be made of them.

While it is altogether too commonly true that salespersons are poor sources of information, there are certain types of advice and suggestions which can be secured together with price information. A salesperson may be told, for example, that a quoted price is too high, and at the same time asked to let the prospective buyer know if any reduction is made. This simple device may result in a subsequent telephone call or postcard offering a better price. For the purchase of clothing it is well to develop a connection with some one salesperson in each of several different stores. Knowing their individual customer's preferences and size requirements, these salespersons may then inform the customer by phone or mail in advance of a specially good buy.

In making use of salespersons it is important to give them your reasons for failing to buy. If you can secure an identical product at another store at a much lower price the salesperson should be so informed. Among department stores it is a common practice to meet any competing price. There is no reason why customers should feel embarrassed; those engaged in selling have genuine respect for buyers who are shrewd enough to know the difference between good and poor quality and between high and low price. It may be unfair but it is generally true that the hardest

[1] Edwards, Alice L., "Information About Merchandise Available to Customers in Retail Stores," in *Journal of Home Economics*, vol. 31, pp. 701–702.

persons to satisfy are usually the ones who receive the best in merchandise, service, and price.

Those persons who buy habitually at one store without ever asking questions form the basis of what merchants call good will. This good will, in the case of large stores, may be valued at hundreds of thousands of dollars. Actually it amounts to nothing more than the probability that patrons will continue to buy at the same store without question. Those prospective buyers who make it a practice to shop around, openly comparing quality and price, form the basis of real competition. They are the modern counterparts of the economic men of which classical economists wrote. If consumers wish to have merchants capitalize their carelessness they will continue their customary buying practices; but if they wish to secure for themselves greater real income by spending more wisely they will emulate the economic man.

In shopping around consumer buyers will find three general types of stores. The most common, with the exception of a few lines of business, are those types of stores commonly known as independent. Usually, but not always, they are small stores and are operated by the owner. The second general type of store, and also second in importance, is that popularly known as the chain. In certain lines of merchandising, chain stores enjoy a very high percentage of the total volume of business, but for all other types of merchandising their volume is smaller than that of independent stores. The third general type of retail store is that known as a consumer co-operative. These are not very common in the United States and consequently their volume of business is probably not more than 1 per cent of the total volume of retail trade. Their number has been increasing steadily, however, and the principles which they practice in business operations are so important a departure from those commonly applied that Chapters 18 and 19 are devoted to a more detailed account.

In the broad economic sense the process of production involves the creation of form, time, place, and possession utilities. All those who are engaged in the extractive and processing industries clearly perform a service for consumers by putting raw materials into a more useful form. Also those who transport processed commodities to the places where consumers want them and those who store them until such time as they are demanded are performing an economic service. The retail merchant often combines the latter two services and in addition creates possession utility by carrying in stock in a convenient location a large supply of things which experience has taught him his customers will wish to have more or less regularly. It costs money to perform these services, and

a large part of the final price which the consumer pays goes to those who render the various merchandising services. Asking themselves the question, "Does distribution cost too much?," a committee of businessmen sought the facts and discovered that the answer is "Yes." Broadly speaking, they found that 59 cents out of every consumer's dollar goes for marketing costs. The Committee suggested many ways in which these costs can be reduced. One of the economic problems to be solved in the future is that of achieving as high a degree of efficiency in marketing as has been achieved in processing.

Sometimes consumers can reduce marketing costs or even eliminate them by performing all or some of the services themselves. For example, a family living in a suburban or rural area may have the choice of having milk delivered on its doorstep or of having someone in the family go after it. If it is delivered in the usual way, the final price of 16 or 18 cents a quart includes perhaps only six or eight cents for the milk itself, the remainder being charged for the services of hauling the milk from the farm to the processing plant, of pasteurizing, cooling, bottling, and delivering the product in conveniently sized containers. If the family goes directly to a near-by farm it may be possible to buy the milk for 6 or 8 cents a quart, take it home, pasteurize it on the kitchen range, cool it in the mechanical refrigerator, and bottle it in whatever containers may be at hand. Performance of these latter services will not entail any cash outlay, although it might be proper to charge 5 cents a mile for operating the automobile and a certain portion of the fuel bill should be charged against pasteurization and a portion of the electric bill likewise charged against cooling and refrigeration of the milk. Even if that were done the final cost would probably be considerably less than the retail price.

Most consumers have no choice but to purchase their products in the established retail market. This means that they have to use independently owned and operated stores and stores owned and operated as part of a chain by a large corporation. For a great many people the question whether or not to deal with chain stores is settled entirely on an emotional basis. There is not room here to enter into the controversy, nor is it necessary, for the reader may turn to any one of several good sources for an evaluation of the two types of stores.[1] Perhaps the fundamental difference between them is that in general the independent stores in addition to handling their line of merchandise render a number of additional services, such as taking orders over the telephone, delivering them, extending credit, and permitting the return of unwanted or un-

[1] Coles, Jessie V., *The Consumer-Buyer and The Market*, John Wiley, New York, 1938; Reid, Margaret G., *Consumers and The Market*, F. S. Crofts, New York, 1942.

satisfactory merchandise. All of these services cost money and someone has to pay for them. It is estimated that delivery service alone costs from 1 to 2 per cent of sales. In one study it was calculated that it cost the retailer 22 cents every time a truck made a delivery. Credit costs run from 3 to 4 per cent of the customer's dollar. Many people want these services and are able and willing to pay for them.

Some stores, on the other hand, operate on the principle that the ultimate buyer wants the retail merchant to act as his purchasing agent, assembling a stock of merchandise in a convenient place to which the buyer himself will go and make selections. Operating on that basis such stores do not ordinarily provide delivery service, telephone service, credit, nor permit the return of unwanted merchandise. As a result, all of the available evidence leads to the conclusion that the cash prices for merchandise of comparable quality in chain stores are lower than in independently owned stores. As a matter of fact, if one could break down the price charged by independent stores into two parts, one for service and one for merchandise, it might very likely be that the independent store price for merchandise would be practically the same as that in the chain. This is not done, however, and consumers who deal with independent stores pay for all those services whether they use them or not.

This brief discussion seems necessarily to lead to the conclusion that one who wishes to be an intelligent buyer cannot restrict himself to any one type of store or to any individual firm. Evidence presented in Chapter 13 indicates clearly that wide price variations prevail. The consumer who wishes to get the most for his dollar will take advantage of those price variations by making his purchases in those places where merchandise prices are lowest, proper account being taken of quality.

Pay Cash and Carry. An important step in developing the art of good buymanship is to shop in person, pay cash for all purchases, and carry the merchandise home. In modern times with so many families owning automobiles there is no good reason why they should have daily delivery of small items. If they follow the method of planning their purchases for the week and buying supplies at one time for such a period they can use their own car and, by paying cash, save additional amounts. Of course on larger items it is necessary to depend on delivery service, but consumers should recognize that that is something for which they must pay.

Personal shopping alone makes possible wise buying. One may use the telephone as a means of securing comparative price information, but to use it for transmitting orders is not usually wise. Still less desirable

is the practice of sending small children alone to make purchases, although it is good practice to let them accompany adult buyers so as to learn proper buying procedure.

After one has planned purchases, shopped around, and located the best buys, the final steps include figuring split prices, and checking weights, measurements, and additions. Many items are priced on the basis of fractional weights and fractional prices. In some cases it is impossible to reduce prices to a comparative basis without pencil and paper. Even then one must be fairly adept in working with fractions. Which is the better buy, medium- or large-size cakes of soap if the medium-size sells at the rate of 6 for 25 cents, while the large cake sells at 3 for 16 cents? Neither one indicates weight. It is necessary to ask the clerk to place them on a scale. One then finds that the medium-size weighs 8 ounces, while the large cake weighs $12\frac{1}{2}$ ounces. Reducing these figures to a comparative basis it is found that the medium-size cake costs 4.16 cents per half pound, while the large size costs only 3.41 cents per half pound. Many similar illustrations of confusion resulting from fractional prices could be given. The wise and shrewd buyers will take time to make necessary comparisons. Also individually and as members of consumer organizations these buyers will insist that manufacturers and merchants package and sell their products in such a way that comparative prices can be figured more readily.

No matter what reputation one's retail merchant may have for integrity it is important always to check weights, measurements, and additions. Even though there is no intent to defraud buyers, mistakes may occur, particularly in those cases where products are weighed on noncomputing scales. Clerks whose education may have stopped with the eighth grade are not infallible in calculating prices. If, for example, bulk cheese is selling at 45 cents a pound and the clerk cuts a slice weighing $14\frac{3}{4}$ ounces, he is no better qualified than the buyer to calculate the exact price of the purchase. Frequently to cover his embarrassment he will state quickly a price at which he has guessed. Evidence is given in Chapter 26 showing the extent to which patrons of stores are victims of short weights and short measurements. Where one buys in large quantities it is all the more important to check additions even though an adding machine may be used. The wise buyer simply must discard any sense of embarrassment at what so many people regard as pinchpenny policies. One may be sure that the businessman with whom one is dealing, and businessmen in general, follow the very practices here suggested for ultimate consumers. From the time an order is placed by the purchasing department of a corporation until the invoice is approved by the accounting department, quality, price, and amount are subject

to constant test and check. If such practices are good for businessmen they should be equally good for consumers.

Do Results Justify the Effort?

It Is Easy to Spend Money. It is indeed easy to spend money, but it is very hard to spend it wisely. If one has plenty of money the effort of developing the qualities of good buymanship may seem too great. But very few consumers find themselves in such a happy circumstance. Most of them find their incomes quite inadequate to satisfy all their wants. By devoting some of their thought and time to the technique of buying they may expand their real incomes. Yet it is surprising how many people plead lack of time as an excuse for foolish buying practices. If one wishes to become a good professional man or businessman he studies his task in leisure time even though that requires forgoing some pleasure. Many people find time to study bridge, dancing, riding, or golf, paying good money for instruction. With much less cash outlay these same people could spend at least part of their leisure time in improving their abilities as good buyers. Women particularly enjoy a good bargain. By training themselves in the art of buymanship they may secure still more and still better bargains. Purchasing agents for business firms must study their field and keep fully informed. While retail buyers cannot devote the same time or energy to each class of their much wider range of purchases, they can nevertheless emulate in a general way the technique of purchasing agents. In the final analysis it is up to each individual to determine whether the satisfaction and savings gained from developing himself as a good buyer are worth the effort involved. For those in doubt it might be well to keep a record for six months or a year of the amount of time spent in purchasing commodities and another record of the number of dollars saved as a result of good buymanship.

Summary

Having adopted desirable consuming standards, individuals can stretch their incomes by developing an intelligent buying technique. Family buying is a task which husband and wife should share. To emulate the mythical economic man the first step in developing wise buymanship is to acquire technical information, using some or all of the sources described in this chapter. The second step is to plan purchases in advance, buying large quantities of seasonable goods in bulk. On larger items purchases must be timed to coincide with a lull in popular demand. A third step in the process of intelligent buying is to bargain for better prices, remembering that this is a one-price country only for those who never bargain. Prospective buyers should shop around, making such use

as they can of salespersons. Finally they should pay cash and carry their own orders, after checking weights, measurements, and additions.

If all consumers purchased in this way, business would be on a sounder basis and buyers would be better off. Whether or not results justify the effort is a question which individuals must decide. Certainly very few people have so much money income that they can afford to waste any part of it, nor is their time so valuable that they cannot afford to study buying technique. The percentage of saving secured by better buymanship is much higher than the rate of interest or dividends paid by banks, bonds, or most stocks.

QUESTIONS FOR DISCUSSION

1. Contrast the buying practices of a corporation purchasing agent with those of a housewife.
2. To what extent does your father participate in the family buying program?
3. How much training and experience had your mother had in purchasing prior to her marriage?
4. Are you convinced that Consumers' Research is reliable?
5. Can you accept the findings and recommendations of Consumers Union?
6. Can you suggest additional services which might be rendered by *Consumers' Guide?*
7. Do your local newspapers ever carry items from *Notices of Judgment* or Federal Trade Commission *Reports?* If not, have you ever inquired why?
8. Can you add any illustrations of savings available as a result of buying large rather than small quantities?
9. What is meant by timing purchases?
10. Have you ever bargained for better prices? If so, with what results?
11. What is the good will of a department store? How is it connected with the failure of buyers to shop around?
12. When making retail purchases do you usually figure fractional prices to ascertain the better buy? Do you check weights and measures? Do you always count your change?
13. Compare the time you have spent during the past six months learning how to buy wisely with the time you have devoted to improving your skill at earning money or in developing a hobby such as bridge, golf, dancing, or riding.

PROBLEMS AND PROJECTS

1. Test the technique of buying suggested in this chapter by using it in the purchase of the next large article you need to buy. Keep a record of the time spent and calculate your cash saving. Allowing for the

satisfaction of knowing that you have secured the best article for your purposes, do you think the results justified your efforts?

2. Assume that you are going to buy a radio, washing machine, kitchen range, vacuum cleaner, refrigerator, or some other household appliance or furniture; summarize the technical information available and indicate which make you would buy.

3. Write a paper on the origin, history, and significance of Consumers' Research, or Consumers Union.

4. Write a critical review of one of the books listed on page 342.

5. Using *Consumers' Guide* as a source of information, select several food items and trace fluctuations in price during the past year; in which seasons should each of those foods be purchased, and in which seasons not?

18

Co-operative Buying: Principles and Practice

The Consumers' Co-operative Movement

Principles of Co-operation. In efforts to promote their welfare, consumers have adopted various politico-economic forms of organization other than capitalism, such as socialism, fascism, and communism. While most Americans are familiar with these words, although not with their significance, many of them have not even heard of the co-operative movement. Yet this is a means of promoting consumer welfare which was initiated nearly a century ago. It has grown up within the framework of capitalism, in both Europe and the United States, and in its present form is a significant factor in the economic life of England, Denmark, Norway, and Sweden. Within the United States this new form of co-operating to promote consumer welfare has assumed increasing importance. Several millions of consumers have turned to this method of organization to eliminate or alleviate what they regard as intolerable evils in the prevailing system. More and more consumer co-operative groups are being organized. Wherein do these groups differ from the customary method of organizing to carry on a business? What are the principles and methods of consumer co-operation?

A consumers' co-operative society is a voluntary association of persons organized democratically to supply their economic needs. Yet the difference between a consumers' co-operative and an ordinary private business venture is much more than a difference in method of organization. There is a fundamental difference in purpose. While the primary purpose of a private enterprise is to make profit, the primary purpose of a co-operative is to perform an economic service for its members.

To ensure performance of this service for all members alike, one of the basic principles of co-operation is that each member shall have one vote regardless of how much capital he may have invested or how many shares of stock he may own. Students familiar with recent developments in corporate organization and control know how the principle of voting according to number of shares held results in control by a small number. Those few, actuated by the desire for personal gain, may use their power

to enrich themselves at the expense not only of consumers in general but of their fellow investors. The principle of one vote per member, with rigid restrictions on the use of proxies, is designed to secure and maintain control by all participants.

The principle of democracy is carried further by the requirement of unlimited membership on a voluntary basis. Not all so-called co-operative societies adhere to this principle, but it is one of the fundamental features of the original Rochdale pioneers, whose principles have come to be regarded as the basis of true co-operation. Many co-operatives that have failed had a membership that was restricted to persons affiliated with some existing fraternal, political, or economic organization. Obviously the principle of democracy in a co-operative society can be exercised only on a voluntary basis, which means that individuals are free to join or to withdraw from the society as they like.

A fourth principle of co-operation is that owners of the capital invested shall be paid only a limited rate of return. The rate actually paid is usually that prevailing for loans involving comparable risk. In countries where the co-operative movement is well established the rate paid on a share of capital is frequently less than that prevailing in the open market. The co-operative idea is that capital, like labor, is only one of the factors of production and should be paid a fixed wage. The real owners and the ones who should benefit most from the success of the enterprise are the consumers who are its patrons.

This leads to a fifth fundamental principle of co-operation; namely, that all net savings shall be divided on the basis of patronage. In contrast with the ordinary corporation, which vests control in those who own or control shares of stock, whether or not they actually have invested any capital, and distributes profits either as dividends on shares held or in the form of high salaries, bonuses, or otherwise to a small group of controlling officials, a co-operative society divides its surplus savings among its members according to the volume of their individual purchases. This is a policy which has long been accepted in the field of mutual life insurance. The co-operator contends that the surplus saving is primarily the result of members' participation as consumer buyers. It cannot be denied that the most efficient management will fail to secure a profit in the absence of buyers. The co-operator contends that it is the buyers who make profits possible and who should share in their distribution.

Experience has taught co-operators the importance of two additional principles. Merchandise must be sold at the current market price on a strictly cash basis if a co-operative is to succeed. The principle is that the individual buyer as a consumer buys from himself as a member of the society, paying a price which will cover not only cost of the merchandise

but overhead costs as well. Since costs vary, the individual pays a price which more than covers the immediate apparent cost. At the end of a quarter or half year all accumulations in excess of actual costs are returned to the members on a patronage basis.

These, then, are the fundamental principles of a true co-operative: its membership is unlimited and voluntary, with one vote per member; owners of invested capital are paid a limited rate of return, while net surplus savings are divided on the basis of patronage; and the goods or services are offered for sale at the current market price for cash only.

Co-operative Methods. As the consumers' co-operative movement has grown, certain characteristic methods have developed. Some of these have resulted from necessity in meeting certain problems and situations, while others have evolved as methods of practice.

One of the first problems met by consumer co-operative societies was that of persons who wished to join yet lacked the small share capital necessary for membership. That problem was met by permitting non-members to become members, on condition that their share of capital, which is usually five dollars, be secured by permitting their patronage dividends to accumulate.

Since the spirit and purpose of a co-operative group differ from those of a corporation organized for profit, and since employees of a co-operative are usually, if not always, members of the society, it is obvious that the relation of the employees to the employer is on a totally different basis. In the usual form of corporate organization the employees play the dual role of worker and consumer, while the employer has a double role as consumer and owner of the enterprise. In a co-operative group the balance of power swings to the consumer. The employee of a co-operative has a triple role as consumer, owner, and worker. Obviously, there should be no exploitation of workers by a co-operative for the sake of profit. A true co-operative society is characterized by fair wages, reasonable hours, and satisfactory working conditions.

Co-operatives, no less than other forms of business enterprise, are subject to the vicissitudes of an uncertain future. Experience and sound business practice have taught consumer owners the importance of maintaining out of their surplus savings a substantial reserve fund to meet contingencies. This is all the more necessary when a co-operative group meets with the opposition of vested interests.

Since the co-operative involves a difference not only in methods but in principles of organization, the necessity of educating members and prospective members in the principles of co-operation is recognized. This is accomplished by using a part of the surplus for educational purposes.

The principle of distributing net surplus savings to members according to their patronage requires the use of an efficient system of cost accounting with regular reports to members. Only by this means can members be assured of efficient management and reasonable costs.

A final feature of the co-operative method is co-operation of one group with another. Co-operation displaces competition among these groups and is accomplished through affiliation of a number of consumers' co-operatives with wholesale co-operatives. All are affiliated in the United States with the Cooperative League, which is national in its scope. The League, in turn, is affiliated with the International Cooperative Alliance.

Contrasts with Capitalism. While the co-operative movement has grown up within the framework of capitalism it is evident that certain of its fundamental principles are in sharp contrast. Whereas the prevailing philosophy of self-interest places the welfare of the individual above that of the group, the philosophy of the co-operative movement recognizes that the welfare of the individual will be advanced by promoting the welfare of the group. Co-operation does not displace the principle of self-interest so much as it supplements it. Under capitalism the doctrine of individual self-interest has often resulted in the practice of promoting one's economic interest at the expense of others; under co-operation economic gain for the individual can only follow economic gain for the group.

Under capitalism the motivating force is the desire to acquire profit. The presumption is that the greater one's profit, the greater is his ability to satisfy his economic wants. The co-operative movement, starting as it invariably does among the lowest-income groups, recognizes the practical impossibility of members of those groups ever acquiring profit. It recognizes also what it regards as the exploitation of that group by those possessing the necessary economic power to acquire profit for themselves. Even in capitalistic theory the consumer is the one for whom the entire system of production is organized and the one who controls it. The deviation of practice from theory has been emphasized in the preceding chapters, and enough evidence has been presented to warrant the conclusion that under the profit system the consumer alone does not guide or control the productive process. The consumers' co-operative movement is based on the very simple principle that the way for consumers to secure what they want is to organize themselves economically. Their purpose in co-operating to operate a grocery store or a filling station is not to make profit, but rather to supply themselves with honest merchandise at a fair price. This is usually summarized in the phrase "production for use" instead of for profit.

The principle of unlimited, voluntary membership with one vote per person is the logical sequence to the purpose for which consumers organize themselves. If it is their own group welfare in which they are interested they can be more sure of achieving it by retaining control of an enterprise in their own hands than by turning it over to some individual outside the group whose primary interest is to secure profit.

While co-operatives do not alter the prevailing method of distributing income to owners of capital and to workers on the basis of productivity, they do change the basis on which the profits of a business enterprise are shared. The capitalist theory awards profits to enterprisers as an incentive and as a reward for assuming risk. Without attempting at this point to evaluate that theory in the light of modern developments, the contrasting co-operative principle may be noted. Consumers become the owners by providing the necessary capital. For hired capital and workers they pay a fixed rate, reserving all surplus for themselves as consumer owners. Distribution of this surplus on the basis of patronage, combined with the principle of democratic control, renders impossible any concentration of the co-operative's wealth or economic power in the hands of a few persons. In an economic system organized entirely on the co-operative basis there would be a much wider distribution of wealth and income.

Similarities Between Capitalism and Co-operation. One of the basic characteristics of capitalism is freedom of enterprise. With certain exceptions which may be ignored at this point, anyone may enter any business or profession he chooses. Whether or not he succeeds depends upon a number of factors, including the number already in that occupation and his own ability. The consumers' co-operative movement in no way alters this principle. Any group of persons may start a co-operative association just as freely as they may organize a corporate form of business.

Another characteristic of capitalism is the firm belief in the principle of free competition. Competition among producers is the force relied upon to secure for consumers a supply of quality merchandise at a fair price. As our economic system has matured there have been increasing restrictions on free competition. These have been imposed not only by the government but also by private enterprisers seeking monopoly for their own gain. Nevertheless, the present system is essentially competitive in nature. In fact, competition in its broadest sense will always persist, regardless of the form of economic organization. This is true because competition results from a scarcity of land, labor, and capital. If all these factors were available in such abundance as to be free there would be no problem of economy. The moment society has to decide whether

to use one of these factors for one purpose or another, the principle of competition enters. In this broad sense competition continues under a co-operative form of economic organization. If, however, competition is regarded in the more usual narrow aspect there would be less of it in a co-operative society and it would be less ruthless and wasteful than in the ordinary capitalist society. There is not so much difference in the outward form which competition would take under a co-operative society as in the purpose to which it would be directed. At present there is a competitive struggle for profit which the co-operative would supplant with a struggle for consumer welfare.

A third characteristic of capitalism which would scarcely be changed under a co-operative system is the institution of the right of private property. Unlike socialism or communism, the co-operative movement entails no legal change in the ownership of wealth. Each individual would be free to acquire and retain wealth for his own use. In practice, however, there would be a wider distribution of the ownership of wealth. There would be also a significant difference in the use to which that wealth would be put. At present individuals can combine to organize a corporation which, as a separate entity, owns wealth. These same individuals might combine to organize a co-operative which likewise would be incorporated and therefore be a legal entity with power to own wealth. The primary difference is that the corporation uses its wealth to secure profit, while the co-operative uses its wealth to render a service. In the one case the performance of a socially desirable service may be incidental, while in the other case it is the main purpose.

Freedom of contract is an essential characteristic of capitalism. This means that any person may enter into any legal contract which he thinks will promote his self-interest. It may be a contract to sell his services or one to sell or rent his economic wealth. Short of selling himself, an individual may dispose of his economic goods and services in any way he sees fit. In a co-operative society this right would not be altered. Rather, the difference in purpose combined with democratic control would render freedom of contract a greater reality than at present.

Distribution of income in a capitalist society is presumably on the basis of marginal productivity. Land, rent, interest on capital, and wages of labor are determined by the contribution made by the least important unit of each of these factors. In practice, there is much variation from this principle. Accepting it, however, as a basis for comparison, it may be said that under a co-operative system sharing of income would continue to be based on the general principle of productivity, with three important exceptions. First, co-operatives have already recognized the principle of limiting incomes. Second, there has been a general recogni-

tion of the principle of a minimum wage. The criterion adopted is the amount required to maintain a decent plane of living. The third difference, already noted, is the distribution of surplus savings on the basis of patronage rather than on the basis of stock ownership.

Historical Development of Co-operation

Co-operative Beginnings in Europe. The modern co-operative movement originated in Rochdale, England, in 1844. Twenty-eight desperately poor weavers pooled their limited financial resources for the collective purchase of groceries. For a year after determining to use that means of improving their economic status they saved their pennies. At the end of that time each of the twenty-eight members had saved a pound. Combining their savings, they fitted up the ground floor of a cotton warehouse as a store and laid in a stock of supplies. The principles and methods of co-operation already explained were gradually evolved by that group and have come to be known as the Rochdale principles. From that meager beginning the co-operative movement has grown until an average of more than one fourth of the population of European countries belonged to co-operative societies before the Nazi regime. With the rise and extension of Nazi power most of those societies were deprived of democratic control and denied the use of co-operative methods. In European countries not under Nazi domination the co-operative movement expanded heavily both in volume and in usefulness to the people during the war. By 1937 there were 127,000,000 members of co-operative enterprises in 61 countries. That year the consumers' co-operatives of forty countries were federated nationally and those forty national federations were united in the International Co-operative Alliance with headquarters in London. The Alliance had a 1939 prewar membership of 72,250,000 in 39 countries.[1]

By 1941 there were 8,750,000 members of British co-operative societies whose retail trade approximated $1,200,000,000.

Co-operative activities have expanded to include not only the marketing of groceries, but also insurance, credit, housing, and health. As co-operatives have grown in number and size their activities have been expanded to include the production of such commodities as flour, bread, tea, electric light bulbs, and a number of other commodities.[2]

[1] Selove, Myrtle M., "Co-operatives in Foreign Countries," in *Monthly Labor Review*, vol. 49, pp. 104–131; also an undated (1943) release of the Committee on International Cooperative Reconstruction of the Cooperative League of the United States of America.

[2] For further information concerning the co-operative movement throughout the world refer to Warbasse, James Peter, *Co-operative Democracy*, Fourth Edition, 1942, chap. 3, Harper & Brothers, New York. For an account of the prewar co-operative

Co-operation in the United States. A year after the Rochdale pioneers started their co-operative, the New England Protective Union was launched. In less than a decade there were 403 participating societies affiliated with the Union. That venture, like a great many others, passed out of existence in the hectic Civil War years. From time to time co-operative efforts have been revived, but the movement has never attracted a large following in the United States. Several reasons have been advanced to explain the lack of development in this country while the movement was growing steadily in other countries. One reason commonly given has been the heterogeneous composition of the American population. By its very nature a co-operative society must be built by a small, homogeneous group. Unlike England, Denmark, Sweden, and Norway, the United States in the nineteenth and early twentieth centuries received millions of immigrants from many lands. Attracted by prospects of economic freedom, immigrants for the most part were concerned primarily with gaining for themselves all that was possible under the capitalist system.

Unlike England and the Scandinavian countries, the United States had vast undeveloped lands and natural resources. In the presence of such lavish natural wealth there was little incentive to economize. Americans developed a traditional philosophy of pioneering individualism, which held that any man had equal right and ability to acquire a fortune for himself. In minds dominated by that philosophy there was little room for the co-operative principle to grow. As one writer has put it, our educational system taught the individual to strive to get ahead *of* others instead of *with* others.

In this background of seething, heterogeneous population struggling as individuals to build up huge private fortunes there developed a philosophy of production as a means to consumers' welfare rather than a philosophy of wise distribution and consumption. The co-operative movement is essentially a philosophy of distribution and consumption which rarely if ever develops in a young, growing nation. Most countries in which co-operation has reached its greatest development are mature nations with limited land and resources and a homogeneous population. Perhaps as the United States grows older and its population increases, consumers' co-operation will grow as it has elsewhere.

In many cases where co-operative societies have been organized in

movement in Sweden see CHILDS, Marquis W., *Sweden, The Middle Way*, Yale University Press, 1936; and for a description of co-operation in Denmark, HOWE, Frederic C., *Denmark, the Cooperative Way*, 1936. For the most recent information available concerning the International Cooperative Movement write to the Committee on International Cooperative Reconstruction of the Cooperative League of the United States of America, 167 West 12th Street, New York, N. Y.

the past there has been an admixture of trade-union activities which have violated certain of the fundamental principles of co-operation. Contrary to the principle of voluntary, unlimited membership, trade-unions have sought to limit membership to members of their own organization. Another mistake which was made frequently was that of attempting to do business on a cost-plus basis. Almost invariably such a practice resulted in failure. Some co-operative experiments were the victims of impractical idealists without experience and improperly grounded in co-operative philosophy. On the other hand, some co-operative experiments have failed in the face of bitter opposition on the part of organized groups of businessmen.

Consumers' Co-operation in the United States Today

Recent Growth. In the Middle West, where farmers suffered depression for many years, co-operation has had a fairly steady growth. After 1929, when depression became nationwide, the co-operative movement grew phenomenally. As unemployment increased and income diminished

TABLE XXIX.—ESTIMATED MEMBERSHIP AND BUSINESS OF CONSUMERS' CO-OPERATIVES, 1942[1]

Type of Association	*Estimated Number of Associations*	*Estimated Membership*	*Estimated Volume of Business, 1942*
Commodity Co-operatives:			
Co-operative stores	3,100	485,000	$129,650,000
Service stations or petroleum co-operatives	1,500	480,000	92,875,000
Farm supplies (less petroleum)	1,149	420,000	355,325,000
Other commodity co-operatives	50	25,000	5,800,000
	5,799	1,410,000	$583,650,000
Service Co-operatives:			
Medical co-operatives	30	15,750	345,000
Funeral associations	40	32,500	200,000
Housing associations	60	3,750	2,530,000
Campus co-operatives	380	110,000	3,750,000
Miscellaneous service co-operatives	150	15,000	160,000
	660	177,000	$ 6,985,000
Specialized Consumer Co-operatives:			
Rural electric co-operatives	700	575,000	16,650,000
Credit unions	10,425	3,000,522	362,779,000
Telephone co-operatives	5,000	330,000	5,485,000
Co-operative insurance associations	1,800	6,800,000	103,375,000

[1] CAMPBELL, Wallace J., *Here is Tomorrow—Consumer Cooperatives in America*, p. 6, The Cooperative League of the U. S. A., New York, 1943.

many consumers sought to alleviate their plight by turning to co-operation as a way out. Throughout the 1930's the consumer's co-operative movement continued to expand. Historically, consumers' co-operation has always grown more rapidly in periods of business depression, but the decade 1933–1943 in the United States has shown that the movement is so firmly rooted that it continues to grow in prosperity as well as depression. In the five years from 1936 to 1941, the volume of business conducted by consumers' co-operatives increased by 90 per cent. Table XXIX shows in statistical form the status of consumers' co-operation in the United States at the end of 1942.

Figures for 1941 indicate for consumers' co-operatives an average membership of 264 per co-operative, a share capital of $8,327, assets of $31,226, sales of $89,153, and a net worth of $20,162.[1]

The gross margin for all co-operative associations in 1941 was 18.4 per cent of sales, while the net margin was 5.5 per cent.[2] A comparison of privately owned and operated filling stations with those owned and operated by co-operatives shows that the private stations had a gross margin of 25.4 per cent of sales compared with 22.8 per cent for co-operatives; total expenses for the private stations were 21.5 per cent of sales compared with 14.7 per cent for co-operatives; the net margin for private stations was 3.9 per cent of sales compared with 8.1 per cent for co-operatives.[3] On the basis of a small sample it appears that patronage refunds for co-operatives amounted to 4.3 per cent of sales in 1941.

If one compares the absolute volume of co-operative sales with the total volume of retail trade the percentage is found to be very small. But perhaps the real significance is to be found in the figures of recent growth. If such is the case and if co-operatives continue to increase as rapidly in number there can be no doubt that the co-operative movement will assume increasing significance in American economic life, but its full significance cannot be measured statistically.[4] The story of how consumer co-operatives broke the fertilizer trust is well known in co-operative circles. Likewise, the way in which co-operative oil associations broke the grip of monopoly by establishing their own refineries is an indication of the economic and of the social significance of this type of enterprise. Moreover, co-operatives are very strong in certain regions such as the Middle West and in certain lines of activity, such as retail food stores and gasoline filling stations. Consumer co-operatives in 1943 owned 8 oil refineries, 25 oil wells, 100 miles of pipe line, 12

[1] United States Department of Labor, *Consumers' Cooperation in the United States in 1941, Bulletin No. 725*, p. 17, United States Government Printing Office, Washington, 1943. [2] *Ibid.*, p. 17. [3] *Ibid.*, p. 25.

[4] Clark, Lincoln, "The Cooperative One-Half of One Percent," in *Quarterly Journal of Economics*, February, 1942, pp. 321–331.

fertilizer factories, 4 sawmills, and so on through a list of 75 mills, plants, and factories.

Reasons for Rapid Growth. The National Industrial Recovery Act of 1933 was a significant factor in the rapid expansion of consumers' co-operatives. Aside from credit unions, the greatest expansion in consumer co-operation occurred in retail marketing of groceries and gasoline. Dr. Paul H. Nystrom, who was vice chairman of the National Retail Code Authority and president of the Limited Price Variety Stores Association, warned his fellow members that the tactics they were following would lead to an increased number of consumers' co-operatives:

> "High prices, dictatorial methods and attempts to drive or force the consumer are just the conditions to start a rapid development of consumers' cooperatives. To anyone who has studied the early development of consumers' cooperatives it is clear that they thrive best and most rapidly wherever the regular channels of distribution are blocked by arbitrary, artificial or inefficient methods of operation."[1]

At the same time Mr. George A. Renard, secretary-treasurer of the National Association of Purchasing Agents, warned leaders in the oil industry that their code tactics would lead to an expansion in the number of consumers' co-operatives: "The recent rapid growth of co-operatives in the marketing of gasoline is causing serious concern to the oil industry. Under the oil code a minimum mark-up of 6 cents a gallon is mandatory in the movement of gasoline through the jobber and retailer to the consumer." Manufacturers in the industry refused to believe Mr. Renard. They contended that the codes themselves were not at fault. The blame in their judgment fell upon the Federal government which "has lent aid and comfort to those who desire to form consumers' cooperatives." This last sentence refers to an effort made by oil men to have co-operative activities curbed by ruling that patrons' dividends were rebates within the meaning of the code and therefore outlawed. The answer to that demand was an executive order which exempted bona fide co-operatives from provisions of industrial codes which were designed to prohibit any patronage rebates.[2]

A second factor in the growth of consumers' co-operatives has been the enactment of enabling legislation throughout the country. In January, 1937, consumer co-operative laws of varying completeness were on the statute books of thirty-two states and the territory of Alaska. Amendments during recent years have in general been liberalizing in nature, widening the fields of business, enlarging the powers of co-

[1] *New York Times*, April 4, 1934.

[2] *New York Times*, April 1, 1934; *Monthly Labor Review*, vol. 38, p. 853.

operatives, and raising their standards. In 1939, for example, the North Dakota legislature created a Division of Co-operatives in the Department of Agriculture and Labor. Its function is to serve "as a source of co-operation and information in the establishment and/or maintenance of co-operatives generally."[1] In the same year New Mexico passed the general consumers' co-operative law using the model statute recommended by co-operative leaders and by officials of the United States Department of Labor. On the other hand, the legislatures of California, Indiana, and Wyoming have repealed their co-operative association acts. The New York law defines a co-operative as an organization conducted "primarily for the mutual help and benefit of its shareholders, employees, and patrons without profit which pays not to exceed 6 per cent on capital and distributes the remainder on the basis of patronage or of labor performed for the society." In general, three to seven persons may organize a co-operative and engage in any lawful business. Most laws limit ownership of capital stock to from one to five shares or the limitation is based on a percentage of the total issued. The liability for debts varies from the amount still unpaid on capital stock to a per capita share of all debts, contracts, and engagements. Statutes in twenty-seven states definitely specify that there shall be only one vote per member.[2]

In addition to enabling legislation, a third factor which may be listed as a definite cause for development of consumer co-operatives is the favorable and encouraging attitude of the Federal government and of a large number of state governments. Difficult as it is to untangle the threads by which the National Industrial Recovery Act, the Agricultural Adjustment Act, and other restrictive New Deal agencies exploited the consumer, it must be recognized that at the same time there were less powerful agencies attempting to protect consumers. Thus we find the apparent paradox of *Consumers' Guide*, a publication of the Agricultural Adjustment Administration, vigorously preaching the doctrine of consumers' co-operation. The United States Department of Agriculture and Department of Labor have helped to spread the doctrine of co-operation. The Labor Department in two of its Bulletins, Nos. 606 and 665, tells consumers how to organize and manage consumers' co-operatives. Periodically during the last decade the Department of Labor has made surveys of the extent and growth of the co-operative movement in the United States.

Indicative of the attitude of states in the Middle West, where co-

[1] *Monthly Labor Review*, vol. 50, p. 94. [2] The Consumers' Project, United States Department of Labor, *Consumers' Cooperative Statutes and Decisions*, United States Government Printing Office, Washington, D. C., 1937.

operation is most deeply rooted, is the action in the state of Wisconsin, which passed a law requiring that a course be given in agricultural and consumers' co-operation throughout public schools from the state university down through the grades. In the future no teaching certificates will be granted in the fields of economics, social studies, or agriculture unless the applicant has studied the co-operative movement.[1]

A final factor in the recent growth of co-operatives is the background of experience which new organizations may use as a guide. In former years the co-operative movement was sporadic in nature, with no central unifying body. That defect was overcome in 1916 by the organization of the Cooperative League of the United States, which among many other functions, serves as a clearing house of information, conducts co-operative congresses, and publishes *Consumers' Cooperation*, a monthly magazine. Whereas new co-operatives formerly had to feel their way and learn by experience, the thousands of new organizations which have recently sprung into existence have the experience of their predecessors available to guide them away from common mistakes. Since about 1938 there has been also a rapid expansion of regional co-operative wholesales. These have performed numerous services for local associations, one of the most important being that of functioning as a source of wholesale supply. As a result local associations may secure practically all of their merchandise from their own wholesales which in turn carry in stock an increasing volume of commodities which have been processed by co-operatively owned and operated factories, mills, and refineries.

Types of Co-operatives. It is, of course, quite possible to organize any form of economic enterprise as a co-operative. There are certain types of economic activities, however, which by their nature particularly lend themselves to this form of organization and appeal to consumers as fields in which great economies can be secured. These include the retail marketing of groceries, gasoline and oil, supplying of credit to consumers, insurance, housing, health, and burial associations, to be discussed in the following subsections of this chapter. Rural co-operatives deal largely in feed, seed, fertilizer, paint, farm implements, and other such commodities needed to operate a farm. Since such co-operatives are designed primarily to meet farmers' needs as producers rather than as ultimate consumers, they are not included in this discussion.

(1) *Retail Merchandising.* Probably 80 to 90 per cent of consumers' commodity co-operatives in the United States are engaged in retail merchandising of groceries, meat, general merchandise, fuel, gasoline, and oil. This is to be explained by the fact that in these fields prevailing competitive methods are extremely wasteful, making substantial savings

[1] *Monthly Labor Review*, vol. 41, p. 990.

possible. At the same time these types of enterprise require comparatively small capital investments. Co-operative ventures in these fields may be undertaken by converting an existing privately owned store or filling station into a co-operative, by leasing a privately owned business, or by organizing a new enterprise as a co-operative. The procedure followed varies according to local conditions. From a social point of view the most economical practice is the conversion of a privately owned business into a co-operative. This renders unnecessary further wasteful duplication of retail facilities. Where it is impossible to use this method, the next most economical means and one which requires less capital is that of leasing a privately owned business. Unfortunately, very few co-operatives have been started in either of these ways.

When opposition of private interests forestalls the use of either of the above methods the only alternative is for consumers to raise enough capital to launch their own enterprise. In such cases bitter opposition on the part of private interests is common. Yet the use of traditional competitive methods has proved less effective against co-operatives than in the case of new private competitors. The methods usually used by those already in the field to quell would-be competitors include price wars and refusal of wholesale supply houses to furnish merchandise. The ineffectiveness of these tactics in dealing with co-operatives is illustrated by the experience of a co-operative filling station in a small western town. Upon the opening of a co-operative station the large privately owned oil companies sought to meet the threat by forcing the co-operative into a price war which would lead to financial failure. The co-operative met each successive price reduction to the point where gasoline and oil were being sold at cost. Realizing their financial inability long to meet such tactics, co-operators held a council and decided temporarily to close their station. As long as members could purchase gasoline from privately owned companies for less than cost they were urged to do so. When the private companies stopped selling at a loss, the co-operative station reopened and eventually won the battle. The private companies' next competitive tactic was to cut off the supply of gasoline and oil in an effort to starve out the co-operative station. This led the co-operative to join with other local consumers' co-operatives in the state to organize a wholesale co-operative to supply all the local groups. Not only were the co-operatives then assured of a supply but they were able also to supply themselves with products measuring up to their own standards in quality.[1]

Private companies under the necessity of competing sometimes place

[1] Fowler, Bertram B., *Consumer Cooperation in America*, p. 28, The Vanguard Press, New York, 1936.

elaborate stations on expensive lots located on heavily traveled roads. This, of course, increases expenses and lowers the margin of profit. Consumers' co-operatives, being assured of the patronage of their members, can place their stations on low-priced back roads. Frequently they are located near railway sites where the receipt of supplies in carloads reduces prices. In these ways costs are reduced and the efforts of privately owned oil companies to levy a toll of 6 cents a gallon on gasoline users is thwarted. Obviously the same methods can be used with effectiveness by co-operatives engaged in retailing and merchandising of other commodities.

(2) *Credit Unions.* Our discussion of installment selling in Chapter 14 showed the need for consumer credit. At the same time it showed the lack of facilities for providing consumers with credit at reasonable cost. A credit union is the co-operative response to the need for consumer credit at low cost. The credit-union principle is simple. It holds that funds necessary to meet the credit needs of any particular group are to be found within that group. These funds are made available for co-operative use by pooling them in a credit union. This is accomplished by the purchase of shares, the proceeds of which are used for short-term loans. The credit union was introduced into the United States in 1909 by Mr. E. A. Filene of Boston. In that year the state of Massachusetts passed a law authorizing organization of credit unions. Employees of the New England Telephone and Telegraph Company organized one of the early unions, which began operations with only $20 as capital. At the close of 1941 there were within that company eight unions whose total loans to members throughout the year amounted to $3,134,807. These loans numbered 18,594 and were made to 9,798 borrowers for an average amount of $320 at an average rate of interest of 3 per cent. Dividends of 3.9 per cent were distributed among 18,603 members.

In 1921 Mr. Filene organized and financed the Credit Union National Extension Bureau. This organization, later reorganized as the Credit Union National Association, has become a national clearing house of information and a strong factor in securing favorable enabling legislation in most of the states. In 1929 there were only 400 credit unions in the country. Many states had not passed the necessary legislation permitting their organization. Since that time all but seven states have enacted enabling laws. As a result of the passage of a Federal credit union law in 1934 it is now possible for consumers in any state to secure a Federal charter even though private interests may have prevented the passage of a state law. Seven or more persons may form a Federal credit union by filing a certificate of organization with the Federal Deposit Insurance Corporation. At the beginning of 1943 there were 4,175 in operation.

Passage of these laws, together with the additional activities of the Credit Union National Association and the need for low-cost consumer credit has resulted in a phenomenal growth in the number of credit unions. The 400 of 1929 had expanded to 10,425 in 1941. There were 3,532,000 members in these associations and the number of loans made in that year was 2,408,000, for a total amount of $363,000,000. Their total assets amounted to $322,000,000, their earnings to $14,000,000, and their dividends to $8,800,000.[1] Evans Clark foresees the possibility of 100,000 credit unions supplying $500,000,000 of credit annually to consumer members.

It is reported that during the depressed 1930's not a single credit union failed. Some 300 organizations were liquidated as a result of extensive unemployment in large industrial centers, but it is claimed that in none of those places was any loss incurred. A study of 264 credit unions chartered in the state of New York from 1914 to 1937 showed that 154 were still operating at the end of the latter year. Of the 110 that had ceased operations, data on 57 were obtainable. Of the 57 which had discontinued 35 had closed voluntarily and 22 had been liquidated by the State Banking Department. Of the 22 whose liquidation was handled by the State Banking Department, 17 were open associations and 5 closed. Total funds available for members of the closed associations were 100.5 per cent, but for the open associations the figure was 80.5 per cent. This indicates that there is a definite trend towards the closed type of credit union because financial stability and soundness of loan policy require that the members know each other well enough to know one another's integrity.[2]

One reason credit union losses are small is that members of credit unions understand their organization and its operation and know that as individuals they share equally in controlling lending policy and practice. This is in sharp contrast to their knowledge of commercial banking practice and their complete lack of control thereof.

Credit union practice requires that a borrower must be a member. The basic principles of co-operation govern organization and operation. Membership fees are small, share capital is available in small denominations, and may be paid for by installments. If applications for loans exceed funds on hand credit unions may borrow from commercial banks up to 50 per cent of their outstanding capital. On the other hand, when funds available exceed demands for loans, unions may deposit their surpluses in other credit unions, banks, or building and loan associations.

[1] "Operations of Credit Unions in 1941," in *Monthly Labor Review*, September, 1942. [2] Wilcox, Francis E., "A Statistical Study of Credit Unions in New York," in *Monthly Labor Review*, vol. 50, pp. 666–667.

As their business has grown there has been an increasing tendency on the part of credit unions to expand their fields of operation by helping members finance the purchase of certain types of commodities. For example, a credit union member wishing to purchase an automobile, radio, or refrigerator may secure cash from his union at a much lower rate than he would be required to pay if he were to purchase on the usual installment plan. The possibilities of expansion in this field of financing are very great.

As Table XX on page 266 in Chapter 14 shows, the interest charges on personal loans to consumers are lowest for savings banks, building and loan associations, and insurance policy loans. Obviously, these sources of credit are open only to consumers who have incomes sufficiently large to warrant savings accounts either with banks or building and loan associations or for the purchase of life insurance. It will be observed that credit unions and the personal loan departments of banks are the next lowest sources of loanable funds for consumers. The usual practice for credit unions is to charge interest on loans at the rate of 1 per cent per month on the unpaid balance. Personal loan departments of banks, however, frequently if not usually, charge $\frac{1}{2}$ per cent per month on the original loan, even though the amount of the loan is reduced monthly. As shown in Chapter 14, this method figures usually to a minimum of 12 per cent a year. But the interest charge which a credit union borrower pays is a gross rather than a net rate. The net earnings of credit union operations in 1941 were more than $14,000,000, from which members received on their share capital dividends amounting to over $8,800,000. This means that the borrowers received a dividend which still further decreased the interest rate on the loan. The way in which this operates is much the same as the way in which "dividends" on life insurance policies make the net premiums lower than the gross premiums. It is estimated that credit union members receive from 4 per cent to 6 per cent on their share capital as dividends, thereby reducing the net cost for loans in some cases to as low as 6 per cent.

A significant development dates from 1935 when the Credit Union National Association organized the CUNA Mutual Insurance Society to provide loan protection insurance. This consists of a policy purchased by the individual credit union whereby the lives of all borrowers are insured for the amount of any balance on a loan which might be due and payable at the time of the death of a borrower. This provides protection for the borrower's estate and for the endorsers on his note. The Society wrote insurance to the extent of $72,000,000 and paid 15,000 claims amounting to $2,500,000 in the first eight years of operation. Approximately 4,200 credit unions are thus insured. The next develop-

ment which the Society contemplates is that of entering the field of providing net cost life insurance to the members of credit unions.

For many years the credit union movement has been concentrated heavily in governmental and manufacturing groups. Other fields in which employees have organized large numbers of credit unions include transportation, public utilities, the food and beverage industry, and education. In recent years there has been a noticeable growth of the credit union movement among the churches of the country. At the end of 1941 it was reported that there were then 378 credit unions among the members of local churches. The largest number of these, 288, were to be found in Roman Catholic parishes, with 68 in Protestant churches and 22 in Jewish congregations.[1]

(3) *Insurance*. Co-operative protection against risk of loss by fire had an early beginning in the United States. Forty years before the first American stock fire insurance company was organized, Benjamin Franklin founded the Philadelphia Contributionship for the Payment of Losses by Fire, a society which is still operating. The Workmen's Furniture Fire Insurance Society of New York has operated some 65 years. For fourteen years it had no salaried employees. Management services were contributed freely until the volume of insurance in force amounted to $1,500,000. From a small group of 44 members with $16,000 of insurance in force, the Society, recently named Workmen's Mutual Fire Insurance Society, Incorporated, has grown to more than 68,000 members carrying more than $90,000,000 worth of insurance.

In recent years there has been notable expansion in co-operative coverage to include practically every form of insurance protection. The Farm Bureau Mutual Automobile Insurance Company has 402,274 policies in force and assets of $10,448,000. As of June, 1943, it was the fourth largest mutual insurer of automobiles in the United States. The Farm Bureau Mutual Fire Insurance Company established in the spring of 1934 had a phenomenal growth in its first decade. With 66,000 policies in force covering fire and tornado hazards to the extent of $300,000,000, it has assets of $1,847,000. One year later, in 1935, the Ohio Farm Bureau purchased a controlling interest in the Life Insurance Company of America. Renamed Farm Bureau Life Insurance Company, it had 50,500 policies in force by 1943 for an amount of $66,000,000. Its assets have shown a steady and rapid growth, then standing at $5,184,000.

In 1940 the Central Cooperative Wholesale and Midland Cooperative Wholesale embarked jointly on an insurance plan. Under the

[1] LANDIS, Benson Y., "The Church and Credit Unions," in *Information Service*, Federal Council of the Churches of Christ in America, vol. XX, No. 41.

auspices of Cooperative Insurance Services, which is the central organization for insurance administration, Cooperators Life Mutual was formed to operate in Wisconsin. A similar association was already in existence in Minnesota. A group life policy is offered to local co-operative associations provided three fourths of their membership joins the group. The premium amounts to one half of one per cent of the Association's previous year's sales. For that amount the lives of all members are insured. In the event of death of one of the members, his beneficiary receives as a benefit a sum varying with the age of the deceased and the amount of his patronage of the co-operative during the preceding year. For example, if the decreased was between 16 and 50 years of age, his beneficiary would receive a sum equal to 50 per cent of his purchases.[1]

In one sense probably most of the insurance in force in the United States is provided on the co-operative basis, since most of the companies are organized as mutuals. In essence a mutual insurance company is co-operative, organized as a non-profit-seeking association. Each policyholder automatically becomes a member and shares in surplus savings according to the amount of insurance held. In practice many of these companies deviate from the co-operative principle of democratic control because of their size or as a result of permitting voting by proxy. In either case it is possible for a small group of officials to perpetuate themselves in office at salaries far in excess of those which would be paid on a true co-operative basis. Moreover, the huge reserves accumulated by large insurance companies have been an important source of capital for private enterprises. These newer co-operative insurance companies are increasingly following the tendency to meet capital requirements for other co-operative ventures by supplying loans from insurance reserves.

Provision of insurance protection on the co-operative plan raises the fundamental question as to the workable size of a true co-operative. Adherence to the principles of co-operation seems to require a comparatively small homogeneous group. When the number in a society becomes unwieldy, democratic control disappears, for in practice a large proportion of the members fail to vote. That failure may result from lack of interest, inability to comprehend the complicated problems, or inability to attend regular meetings. Probably the first and third of these are the most common causes for control falling into the hands of an interested few, and if those few are thoroughly imbued with the co-operative spirit no undesirable results may follow, but there is always the danger that such power may be perverted. Out of their years of sympathetic interest and study of the co-operative movement, Sidney

[1] United States Department of Labor, *Monthly Labor Review*, vol. 54, p. 688.

and Beatrice Webb particularly emphasize this danger.[1] Facing this problem of lack of democratic control, the Cooperator's Life Association, an association formed in 1934 with headquarters in Minneapolis, has set up a plan for district meetings and local meetings at which voting delegates to the annual meetings would be selected.[2]

The principles of sound insurance, on the other hand, are best applied over a wide geographic area involving large numbers of insured. As in the case of other large-scale enterprises it may be that co-operation can be carried out only on a compulsory basis. This is the conclusion reached by the Webbs, although its validity is denied vigorously by Dr. Warbasse, dean of the co-operative movement in the United States. The Webbs contend that small, local co-operatives must be supplemented in the case of large-scale enterprises by co-operation on a compulsory basis in which every citizen *per se* is a member, sharing control through his political vote. This means a socialist state, yet democratic control may fail under such a plan if citizens for any reason fail to exercise their voting privilege. Mr. Childs's description of co-operation in Sweden offers encouragement to co-operators in other countries. His study suggests that perhaps the evolutionary growth of co-operation will develop a body of leaders whose concern for consumer welfare is greater than their desire for personal gain.

(4) *Housing*. Provision of housing facilities is a field in which co-operatives have only just begun to develop. Until recent years co-operative housing projects were confined exclusively to apartment dwellings in urban centers, chiefly New York. Since 1939 there has been an extensive development of co-operative low-cost housing projects in such widely scattered areas as Penn-Craft, Pennsylvania; Iona, Idaho; Chapel Hill, North Carolina; Madison, Wisconsin; Greenbelt, Maryland; Minneapolis and St. Paul, Minnesota. By 1940 one hundred fifty-seven had been completed.

Among these projects Amalgamated Clothing Workers have pioneered in building co-operative apartment houses in New York. Sponsored by the Amalgamated Clothing Workers Union, the Amalgamated Housing Corporation has operated as an independent co-operative entity. One of the first projects was that of Van Cortlandt Park, which consists of 638 units containing 2,441 rooms. Another downtown project has 237 apartments and 930 rooms. Stock is sold to prospective tenants to the extent of $500 per room. A third project in the Bronx is a 6-story structure with elevator service, mechanical refrigeration and garbage

[1] Webb, Sidney and Beatrice, *Consumers' Co-operative Movement*, chap. 5, p. 305, reprinted by the authors in 1930.

[2] United States Department of Labor, *Monthly Labor Review*, vol. 56, p. 507.

incinerators. At the end of 1941 another housing project was built by the A. H. Consumers' Society. This consists of 48 units, having 128 rooms. The average rental as of August, 1943, was $11 per month in one unit, $12 in another, and $12.22 for the downtown apartment.

The occupants of these co-operative apartments are members of other co-operative enterprises, such as grocery stores, milk routes, laundry routes, bus service, electric generating plant, and a credit union. Since the first co-operative building was opened in 1927 the tenant members have received over $100,000 in patronage refunds.[1]

All of the houses constructed co-operatively in Pennsylvania, North Carolina, Wisconsin, Maryland, and Minnesota are single-family dwellings, most of them being of frame construction. In two of the projects some or all of the building work was done by the members and by the exchange of labor; in the other projects a private contractor constructed the buildings under association control. Monthly carrying charges on a typical house in the Chapel Hill project are $23.34 for buildings which cost twenty-five cents per cubic foot. In St. Paul the average monthly rental is $35 with a maximum of $40, which includes amortization at 5 per cent, and taxes. In Minneapolis the average house costs $4700 and rents for $32.50 a month, which includes amortization, interest, taxes, loan insurance, and fire insurance. The average income of the members of that group is $1700 a year.

None of the foregoing projects includes the final characteristic of Rochdale co-operative housing, which requires that permanent retention of the title to land and dwellings be held by the Association. Failure to follow this principle is attributed largely to the inability to finance a project on a completely co-operative basis.[2]

Surveys made by the Department of Labor reveal considerable disparity in practice among these co-operative housing ventures and rather extensive deviation from the basic principles of true co-operation. In a real co-operative the members do not receive title to the apartment or house; rather they own capital stock equal in value to the value of the apartment or residence. The title remains in the society and the whole building is owned co-operatively. Another co-operative principle applied to housing requires that members should never be allowed to sell their apartments or houses at a profit. Rather, members sell their stock back to the society for an amount equal to that which they paid for it, minus any deduction for damage. A survey of co-operative practice revealed that in all but four cases the member gets no title but merely leases his apartment. On the other hand, several housing co-operatives

[1] *Ibid.*, vol. 53, p. 646.

[2] Parker, Florence E., "Cooperation in the Building of Homes," in *Monthly Labor Review*, vol. 52, pp. 292–321.

permit members to sell for whatever price they can get, and six societies permit voting according to the number of shares rather than limiting votes to one per member. In one co-operative apartment several units were occupied by non-members.

American experience with co-operative housing is so limited that no conclusion seems justified. The apartment units in New York have been successful and the development of scattered housing projects within the past five years may indicate the beginning of a larger development. As is shown in Chapter 22, there is very great need for housing and it seems quite likely that consumers' co-operative associations will supply increasing numbers.

(5) *Health.* Like housing, co-operatively provided care of health is more a promise than a reality in the United States. In foreign countries notable achievements are accredited to health co-operative ventures. Thus far American experience is limited to scattered ventures. The story of Group Health Mutual of Minnesota provides a typical record of the problems encountered by groups of consumers seeking to provide medical care co-operatively. Almost invariably such groups encounter the formidable opposition of the American Medical Association and its numerous county associations. In Minnesota it was necessary for a small determined group of consumers to raise the necessary capital to organize an insurance company. Having worked out a plan acceptable to 18 doctors operating a clinic in Minneapolis, the group had to start all over again when the Henepin County Medical Association refused to approve the plan. An arrangement was finally worked out under which several hundred members now have medical care in addition to the several thousand who have provision for hospital care. Under the Minnesota plan medical care for the employed head of the household is provided up to the extent of $1000 a year, and medical care to the extent of an additional $1000 for all of his dependents. A family of three or more pays $3.75 per month the first year and $2.75 per month after that. In addition, special payment at the time of medical service is required for dependents, but not for those who are employed. These rates range from 50 cents for office calls to $30 for a major operation.[1]

A most striking and successful health co-operative is the co-operative hospital at Elk City, Oklahoma. In that town of 7,000 population the hospital was financed under the leadership of Dr. Michael Shadid, who had studied co-operation and medicine here and abroad, by the sale of capital stock at $50 a share. The annual cost for a family of four is $25. This includes periodical medical examinations, treatments, surgical

[1] JACOBSON, George W., "The Story of One Health Cooperative in the Making," in *Consumers' Cooperation*, pp. 58–62, April, 1943.

operations, and dental care together with room, board, and nursing while receiving service. The hospital has a staff of seven doctors, two dentists, and twenty-five nurses.[1]

As a result of its involvement in a lawsuit which was carried to the Supreme Court of the United States, Group Health Association of Washington, D. C., has attracted national attention. Organized in 1938 by government employees, Group Health had 3,375 members at the beginning of 1943. The total number eligible for medical care included adult dependents and child dependents for a total of 8,332. Membership dues are $2 per member, $2 for each adult dependent, and $1 for each of the first three child dependents, with no charge for others. For this payment those eligible for care are entitled to "medical and surgical examinations and treatment, including service for refractions of eyes; laboratory tests at the clinic, X-ray examinations at the clinic; surgical operations and confinement cases; professional consultation; ambulance facilities; house calls; and hospitalization in a semi-private room for a period not to exceed forty days for any member or dependent in any one calendar year or in any one illness or in any continuous period of hospitalization." In addition, members are entitled to house calls upon the payment of $1 to cover travel expenses if they live within eight miles of the clinic. As a result of opposition to Group Health the American Medical Association and the District Medical Society were indicted in December, 1938, on the charge of conspiring to violate the Sherman Act by restraining trade or commerce in the District of Columbia. Through four years the case was fought in the courts, finally reaching the Supreme Court of the United States, where the conviction by the lower court was upheld. Heretofore, the opposition of the American Medical Association has been a deterring factor in the development of co-operatives for medical care. The decision of the United States Supreme Court "may play a major role in opening the way for development of co-operative medical service plans in the United States. . . . "[2]

As of May, 1943, the Bureau of Labor Statistics reported thirty-five medical co-operatives in operation, with indications of continued growth.

Co-operative care of health holds very great possibilities. Under the

[1] Shadid, Michael, *A Doctor for the People*, The Vanguard Press, 1939.

[2] This paragraph is based upon information drawn from *G. H. A. News*, published by Group Health Association, Washington, D. C.; the by-laws of the Group Health Association, Washington, D. C., April 4, 1943; the decision of the Supreme Court of the United States in the case of American Medical Association *vs.* the United States of America; and private correspondence with the Secretary-Treasurer of Group Health Association.

present system many people whose medical requirements are the greatest are the ones least able to pay. Unlike housing, the capital necessary to finance a hospital is not necessarily large per member, while in the case of co-operative provision of medical care without hospital service there need be no capital cost at all. From a social point of view an extension of co-operative health care would be a significant force in building up and maintaining national health. Preventive rather than curative action might become customary. Dividends in national health would be immeasurable.

(6) *Burial Associations*. It is not surprising that alert consumers have sought to reduce burial costs through co-operative action. As in the case of housing and health, developments thus far are limited, but possibilities are great. Continued growth of burial associations resulted in a weak attack by the Minnesota State Undertakers Association. A writ of mandamus was secured preventing the Secretary of State from filing articles of incorporation for burial associations. Minnesota law defines a co-operative as "a group of ultimate consumers and/or producers organized on a co-operative plan." The Attorney General interpreted the law to mean that co-operative burial associations could not be organized legally since the ultimate consumer would be a dead person![1]

In spite of such opposition, the number of associations continued to increase, with 40 in operation at the end of 1942. These associations are located mostly in Iowa, Minnesota, Nebraska, South Dakota, and Wisconsin, and number 32,500 in their membership. The membership fee is usually $5. In contrast to the average cost per funeral of $363, members of mid-western burial associations paid an average of $166 for funerals in 1939. That figure covered a complete funeral, including embalming, funeral direction, casket, use of the hearse, the lowering device, and the grave cover. Most of the associations own or lease quarters in which they have chapel, casket room, and embalming room. Generally they have their own hearse and the larger ones employ a full time undertaker who also acts as manager of the association.[2]

(7) *Campus Co-operatives*. One of the most notable developments in consumers' co-operation in recent years has been the rapid growth of co-operatives among college students. The first official survey made by the United States Bureau of Labor Statistics disclosed some surprising facts. At the end of 1942 there were some 380 active student consumer co-operatives, operating on 134 campuses, in 44 states. There were

[1] *Monthly Labor Review*, October, 1931, p. 79. FOWLER, *op. cit.*, p. 154. *Consumers' Cooperation*, July, 1935, p. 133.

[2] United States Department of Labor, "Operations of Cooperative Burial Associations, 1939," in *Monthly Labor Review*, November, 1940.

110,000 student members engaged in operating book and supply stores and providing themselves with living quarters and meals. The 1942 volume of campus co-operative business was approximately $4,000,000. The net earnings of 132 reporting associations amounted to $230,331, and patronage refunds to $133,437 in 1941. *The Campus Co-op News Letter* is issued monthly during the academic year by the Cooperative League of the U. S. A.[1]

Summary

The consumers' co-operative movement has developed within the framework of capitalism as a technique for promoting consumer welfare. Co-operative principles include unlimited, voluntary membership with one vote per member, a fixed return to capital, cash sales at current market prices, and distribution of net savings according to patronage. Co-operative methods permit members to pay for share capital out of patronage dividends, and workers, as members, share in control. Well-managed co-operatives build up a contingent reserve, use a cost-accounting system, and co-operate, through central co-operatives, with other co-operative groups.

In contrast with capitalism, the consumer co-operative movement emphasizes group welfare, produces for use instead of for profit, and provides democratic control. Free enterprise, free competition, in a broad sense, the right of private property, and freedom of contract are characteristic of co-operation, as of capitalism.

The heterogeneous, individualistic population of the United States, possessed of abundant natural wealth, has not offered a fertile soil for growth of the co-operative movement. But conditions have changed rapidly in the last generation, and co-operation has grown phenomenally. Today consumers' co-operation is a definite feature of American economic life, with thousands of co-operatives engaged in retail merchandising and consumer banking. Other fields include insurance, housing, health, and burial associations.

QUESTIONS FOR DISCUSSION

1. How much did you know about consumers' co-operatives before reading this chapter?
2. If your father (or some other relative or friend) operates a retail store or filling station, compare his organization, motives, and methods with those of a consumers' co-operative.

[1] *Monthly Labor Review*, vol. 56, pp. 703–709; *Consumers' Cooperation*, June, 1943, p. 88; *Campus Co-op News Letter*, The Cooperative League of the U. S. A., 167 W. 12th Street, New York.

3. Is the consumers' co-operative movement socialistic? Communistic? Un-American?
4. Why, do you think, has the consumers' co-operative movement grown less rapidly in the United States than in England? Why, do you think, has it taken root more deeply in certain sections of this country than in others?
5. Is a governmental attitude favorable to consumers' co-operatives desirable from the co-operators' point of view? Compare this situation with that of a government favorable to organized labor; also with organized capital.
6. Why are most consumers' co-operatives engaged in retail merchandising of groceries and gasoline?
7. How does a credit union differ from the personal loan department of a bank? From a personal finance company?
8. Can sound insurance be written on the co-operative plan?
9. In view of the great need for new housing in the United States why are there not more co-operative housing projects?
10. In what ways do "state medicine," "contract medicine," and co-operative health care differ? Assuming a change from the present system, which plan would you prefer? Why?

PROBLEMS AND PROJECTS

Problems and projects on the co-operative movement are given at the end of the following chapter. Read them now, in advance, especially Projects 4, 7, and 10, so that any necessary letters can be written without delay.

19

Co-operative Buying: A Critical Analysis

The Labor Movement and the Co-operative Movement

Consumers or Producers? Obviously, every man, woman, and child is a consumer. In the most prosperous peacetime periods so far not more than 54,000,000 of the 136,000,000 people in the country have been gainfully employed. In depression periods the number of those gainfully occupied has dropped to 35,000,000 or less. Figures have been given showing that about 16,000,000 of the 33,000,000 families received incomes of less than $1,500 each in 1942.[1] These are the conditions after generations of effort on the part of workers to increase their money incomes by means of labor organization. In accordance with traditional American philosophy, workers have concentrated their attention primarily on efforts to secure higher wages. Almost without exception efforts of labor organizations have been directed to securing recognition of the right of collective bargaining in the hope that through that method higher wages, shorter hours, and better working conditions might be secured. The underlying idea seems to have been that their interests as consumers were to be promoted chiefly by improving their status as workers. To a considerable extent that idea is sound. So far as it goes, it is a perfectly legitimate philosophy, but it does not go far enough. It assumes that an increase in money wages will result automatically in greater real income for them as consumers. It ignores entirely the great need for families in lower-income groups to know more about the business of living. It fails to recognize that a 10 per cent increase in wages may do no more than preserve the family real income in a period of rising prices. As a matter of fact, it may not even succeed in doing that. It overlooks entirely the possibility of increasing real income by other methods. It does nothing to protect workers as consumers against the power of modern advertising and high-pressure salesmanship fortified by the device of installment selling. It makes no provision for guarding against the purchasing of unnecessary, unwholesome, fraudulent, misrepresented merchandise. It makes the mistake of creating and perpetuating an artificial distinction

[1] See page 309.

between workers as producers and workers as consumers. Actually the ones gainfully employed are playing a dual role in which their interests should coincide. As a matter of fact, they often conflict. Higher wages to workers are often cited as an excuse for raising prices to consumers. As consumers, workers are interested in an abundance of wealth at low prices; as producers they are interested in a scarcity of goods and services to yield high prices. In sheer numbers, families represented by gainfully occupied workers in the lower-income groups represent a dominant proportion of the entire population. This means that their interests as consumers take precedence over their interests as producers. When this simple truth dawns on American workers it may be expected that the labor movement will expand its activities to include a consumer movement.

The American labor movement has developed primarily along craft lines. While this has served to identify the interests of small groups of men doing similar work, it has served to intensify the conflict of interests with other small groups of men and with that vague body of inarticulate consumers. Sporadic efforts have been made from time to time to develop consumers' co-operatives in conjunction with craft unions; but those efforts have failed. The failure has resulted from efforts to restrict membership to those affiliated with a particular craft union. Unsuccessful efforts were made to divide consumers artificially into groups having a chief community of interests as workers. This was in direct opposition to the idea that the interests of all consumers are fundamentally similar. In short, an effort was made to create a conflict of interests where none existed. Perhaps development of industrial unionization in the future may eliminate some of these conflicts.

A second reason for the failure of consumers' co-operatives identified with craft unions was the usual tendency to regard the co-operative merely as means to an end rather than as an end in itself. In popular parlance, workers are inclined to be fair-weather co-operators. If temporarily they could buy their supplies at a lower price in a company store they were quite likely to do so without questioning the probable long-run results. To them the co-operative was merely a store where they expected to buy a sack of flour for less than they would have to pay elsewhere. Rarely was there any realization that co-operation, like labor organization, is a movement. This was due primarily to the lack of co-operative education on the part of leaders as well as members.

Although there has been a definite labor movement in the United States for more than eighty years, an amazingly small proportion of gainfully occupied workers are found in the ranks of union members. Probably not more than 25 per cent of workers eligible for union mem-

bership belong to independent labor organizations. If the numbers affiliated with company unions are included, and it is doubtful whether they should be, the percentage is raised somewhat, but not very much. Not only is the number of organized workers small, but membership in independent unions is limited largely to skilled and semiskilled workers. The industrial unionization movement has drawn in some unskilled workers but, practically speaking, the low-wage, unskilled American worker remains unorganized. Yet it is among such workers that the need is greatest. What consumers' co-operatives can accomplish for such workers is illustrated by the experience of 215 Negro workers in Chicago. Composed largely of government employees, school teachers, railroad workers, and some professional people, this group started as a study club in October, 1936. Their one point in common, in addition to being consumers, was that they all lived in the same apartment house. Within a few months a buying club was started and in June, 1937, a store was opened. Carrying a complete line of groceries, produce, and meat, the store did a business of $55,000 in 1942. The average income of the members varies from $1,800 to $2,000 a year.

In recent years there has been a very sharp increase in the number of co-operatives organized in industrial areas. There are something over 100 consumer co-operatives in which the members of labor unions are prominent as members and officers.[1] When Donald Montgomery resigned in protest as Consumers' Counsel in December, 1942, he was immediately engaged by the National Office of the United Automobile Workers to serve as Consumers' Counsel for that union.

In their 1941 annual conventions, both the American Federation of Labor and the Congress of Industrial Organizations adopted resolutions pertaining to consumers' co-operation. The American Federation of Labor directed its Executive Council to "give consideration to the subject of consumers' co-operative activities and to production in consumers' co-operative organizations." The Congress of Industrial Organizations instructed its officers to "undertake a careful analysis of ways and means whereby the CIO and its affiliated organizations may participate in the development of the consumers' co-operative movement and stimulate the interests and activities of union members along such lines."

Consumers' co-operatives do not cut wages in order to cut prices. Good wages and working conditions are basic in a Rochdale Co-operative. A study made by the International Labor Office shows such conditions do exist in most foreign countries. But the co-operative movement in the United States has not yet developed a real personnel policy.

[1] Myers, James, *Labor and Co-ops*, The Cooperative League of the U. S. A., New York, 1943.

Relationships between workers and associations are good, but as the size of the co-operative grows there is need for machinery to deal with disputes. The latest survey of wages and hours among consumers' co-operatives was made in 1936. At that time it was found that with respect both to wages and to hours consumers' co-operative workers were somewhat less favored than those in private business. The average annual earnings of consumer co-operative workers were $1,155. On a weekly basis it was found that workers in consumers' co-operative retail stores averaged $19.04 while those in privately owned stores averaged $20.17. Employees of privately owned and operated filling stations averaged $24.95 a week compared with $23.54 received by co-operative employees. On the whole co-op employees were 5 per cent below the wage level found for private employees. It was pointed out, however, that these averages include manager's wages as well as those for the clerks and that 72 per cent of the co-operative retail trade is conducted in towns of less than five thousand population where living costs are undoubtedly relatively low.[1] Consumers' Cooperative Services in New York City has long been in the vanguard in its wage and hour policies. In July, 1942, when the basic union scale in privately owned cafeterias was reported to be $16 per week for a forty-five hour week for women and $18 for a forty-eight hour week for men, Consumers' Cooperative Services was paying its workers a minimum rate of $22.70 for a forty-eight hour week.[2]

The main conclusion to which this discussion leads is that the labor movement and the co-operative movement are supplementary. The future holds great possibility for a revitalized labor movement whose leaders and members recognize the place and significance of consumers' co-operation. The low-income workers need both these movements. Perhaps the future may see the development of a combined labor-co-operative movement which, together with political action, would make for a powerful consumer-citizen-worker alliance.

Is Consumers' Co-operation a Threat or a Promise?

Attitude of Businessmen. Before 1935 American businessmen were either unaware of the co-operative movement in the United States or regarded it with tolerant amusement. Examination of the contents of *Business Week* and *The Nation's Business*, two typical publications representing the businessman's point of view, revealed scarcely any articles dealing with consumers' co-operation prior to 1935. In that year there was a steadily increasing number of columns devoted to what business-

[1] United States Department of Labor, *Monthly Labor Review*, vol. 47, pp. 485–499.
[2] *Ibid.*, vol. 56, p. 509.

men regard as a new threat. Since then scarcely an issue of *Business Week* has failed to include some comment on co-operation.

Roger Babson has warned merchants that they may be "sitting on dynamite." They were told that a few years ago if anyone had forecast a consumer uprising in this country the whole idea would have been denounced as a false alarm, but now Mr. Babson is not so sure. This new consumers' movement has certain elements which are fundamentally sound: "It has something of truth and crusading quality almost like a spiritual revival. . . . Potentially it has enough votes, enough money, and enough economic soundness to split things wide open. . . . If consumers ever get organized and go into real action, our present retailing, wholesaling, and producing systems might be blown to bits." As four kegs of "dynamite" on which merchants may be sitting, Mr. Babson referred to the increasing power of consumers in Washington, the persistent efforts to tighten up food and drug laws, consumers' advisory services such as Consumers' Research, and consumers' co-operative societies. Mr. Babson concluded that "We all must watch our step if consumers ever become wise to their latent power and decide to become dictators in *fact* as they already are in *theory*. We say, and earnestly, that merchants who laugh off these consumers' crusades are sitting on dynamite."[1]

In the same vein Mr. C. H. Janssen told readers of *The Nation's Business* that "it has not been many years since the food and grocery industry looked with tolerant amusement upon the efforts of a few daring souls to establish retailer-owned co-operatives. Wholesale grocers scoffed at the idea, sought to deny co-operatives' access to sources of merchandise. Manufacturers refused to sell to them. But few will deny them now. In fact, their favor and patronage are being courted and sought. As they gained experience and able management, they made rapid progress. . . . Private enterprise has been too busy warring within its own ranks to pay much attention to this new rival."

As these quotations show, and many others are available, there is a growing fear, on the part of retail merchants, of this new rival of proved efficiency. As expressed in *Business Week*, "Particularly disturbing to retailers now is the improved efficiency with which co-ops are operating." On the basis of reports made by 42 consumers' co-operative stores, it was found that their typical net sales were $50,000, the net cost of merchandise 81.5 per cent, leaving a gross margin of 18.5 per cent. By comparison 34 chain food stores had typical net sales per store of $41,000 and operated on a gross margin of 22.94 per cent. Co-operative salaries and wages accounted for 9.6 per cent of sales compared with 12.13 for

[1] BABSON'S *Reports*, November 25, 1935.

chains; total expense before interest was 16.6 per cent for co-ops compared with 22.26 per cent for chains; net profit was 0.9 per cent for co-ops compared with 0.14 per cent for chains. The rate of stock turnover for co-operatives was 12.8 compared with 8.13 for chains.[1]

It is sometimes charged that consumers' co-operative stores pay out less in taxes than do stores privately owned and operated for profit. A comparison of tax payments by the two types of stores showed that private independent merchants operating grocery stores paid total taxes in 1938 amounting to 1.27 per cent of total sales compared with 2.93 per cent paid by co-operative grocery stores in 1940. Total taxes for private grocery and meat stores came to 1.52 per cent of sales compared with taxes of 3.16 per cent for co-operatives. Corresponding figures for country general stores were 2.07 and 2.17 while those for gasoline filling stations were 1.48 for the privately operated stations compared with 2.24 per cent for co-operatives. Some of these differences may be due to possible tax changes between 1938 and 1940, the years used for comparison. Another possible explanation is that co-operatives have a larger paid labor force, consequently pay higher social security taxes.[2]

Burley concludes that consumers' co-operatives' operating costs are lower than those of private trade in parallel lines. Wages and salaries comprise the largest expense factor in co-operatives, which, according to Burley, is due to the fact that wages average slightly higher than in private business. Rental costs are lower for co-operatives than for similar types of private stores. The advertising expense ratio is much lower. Although co-operatives extend credit almost as freely as private stores, their losses from bad debts are unusually low. Delivery expenses are low or non-existent.[3]

A Federal Trade Commission report in 1943 shows retail consumer co-operative marketing costs to be the lowest per dollar of net sales in the retail field. Compared with 22.58 cents per dollar for independents and 20.62 cents for chains, co-operative costs were 19.50 cents.[4]

A seventeen-year survey (Table XXX) indicates that retail store and gasoline-filling-station co-operatives are gaining in sales, in net earnings, and in the volume of patronage refunds. The oil co-operatives show an unusually strong record.

[1] Schmalz, Carl N., *Operating Results of Consumer Co-operatives in the United States in 1937*, pp. 5, 10, Harvard University, Graduate School of Business Administration, Bureau of Business Research, Boston, 1939.

[2] Parker, Florence E., and Zorach, Pessim, "Taxation of Consumers' Co-operatives," in *Monthly Labor Review*, vol. 54, pp. 968–988.

[3] Burley, Orin E., *The Consumers' Cooperative as a Distributive Agency*, pp. 233–236, McGraw-Hill Book Company, New York, 1939.

[4] Federal Trade Commission, *Methods and Costs of Distribution*, Part 1, "Important Food Products," p. 3, November 11, 1943.

TABLE XXX.[1]—INDEXES OF SALES, NET EARNINGS, AND PATRONAGE REFUNDS OF STORE AND PETROLEUM CO-OPERATIVES, 1925–1941
1929 = 100

Year	Retail Store Associations			Petroleum Associations		
	Sales	Net Earnings	Patronage Refunds	Sales	Net Earnings	Patronage Refunds
1925	82.3	84.0	88.1	38.6	34.5	30.3
1926	88.3	90.2	82.6	54.0	51.3	54.8
1927	93.0	89.9	91.5	62.9	52.0	51.0
1928	98.1	94.5	97.3	79.4	51.7	57.4
1929	100.0	100.0	100.0	100.0	100.0	100.0
1930	97.4	97.4	93.1	114.6	145.2	146.6
1931	76.7	65.6	82.7	103.5	111.7	120.4
1932	59.7	30.2	83.3	95.0	79.2	101.3
1933	55.5	34.3	58.1	93.4	74.5	101.6
1934	64.2	54.0	81.8	114.9	86.2	122.1
1935	75.2	60.8	92.5	142.9	94.7	142.7
1936	87.5	87.6	129.8	168.8	115.7	173.9
1937	101.4	90.8	149.3	203.7	146.0	212.2
1938	95.5	86.3	129.7	209.0	143.1	226.4
1939	100.0	96.6	177.7	214.6	143.4	233.9
1940	113.6	112.3	173.3	232.0	165.1	288.4
1941	129.5	142.2	192.4	293.2	213.0	363.1

In the face of such figures as these and reports of phenomenal growth in the number of co-operatives it is not surprising that retail merchants no longer regard the co-operative movement with tolerant amusement. Their fears are heightened by a growing realization that ordinary competitive methods fail to stifle this new rival. With lower operating costs co-operatives can withstand price wars, while efforts to cut off supplies only result in the organization of their own wholesale supply houses. European, and recent American, experience shows that the refusal of manufacturers to sell to wholesale co-operatives results in extension of the co-operative principle to manufacturing. The Curtis Publishing Company concludes its report of a survey of the co-operative movement in the United States in 1943 in these words: "The cooperative movement presents an immediate and urgent challenge to business . . . which has important implications for the post-war period. If the movement continues to increase . . . business firms will be forced to realize that cooperation is not an additional way of doing business, but an important competitor to the profit system."[2]

Can Businessmen Reform the Competitive System? Will the reaction of

[1] *Monthly Labor Review*, vol. 47, p. 236, for 1925–1936; United States Department of Labor, *Consumers Cooperation in the United States in 1941*, Bulletin No. 725, p. 33, for 1937–1941.
[2] *Tide*, p. 92, September 15, 1943.

businessmen to consumers' co-operation be positive or negative? Will they attempt to meet this new form of competition by obstructionist tactics or by attempting to reform the present system in the interests of consumers? Two writers already quoted offer their own suggestions. Mr. Babson believes that one immediate safeguard is to modernize advertising and merchandising. In his judgment consumer rebellion can make little headway when businessmen themselves take the initiative and put character into their production and publicity. Those suggestions are so vague as to be of little help to individuals concerned with this new problem. Mr. Janssen is much more detailed and specific. He believes the first step is for business to quit washing its dirty linen in public. He does not believe that the cost of distribution can be reduced materially, nor that a more orderly flow of goods can be facilitated by consumers' co-operatives. On the other hand, he thinks the elimination of private incentive and individual initiative would prove a definite social loss. Mr. Janssen presents a seven-point program to be followed by wholesale and retail distributors of groceries, but his proposals for the most part do not go to the root of the trouble. Merely washing dirty linen in private and refusing to recognize proved efficiency will not solve the problem. Educational campaigns to inform consumers of the virtues of the present marketing system will scarcely succeed if based only on wishful thinking. Both are nearer the truth in recognizing, as Mr. Babson does, the economic soundness of co-operation and in admitting, as Mr. Janssen does, that the final decision will be made by consumers.

There is one group of private businessmen, however, who have indicated that they expect to make a vigorous fight against the continued spread of consumers' co-operatives. Organized first as the League for Protection of Private Enterprise, the new organization has incorporated under the title Central Coordinating Group, Inc., with headquarters in Chicago. Leaders in the group represent grain, lumber, oil, coal, furniture and hardware companies, retail clothiers, dairy groups, and meat dealers. The program of this new group is clothed in some secrecy and is as yet incompletely formulated. Information available indicates that they intend to attempt to secure state and Federal legislation which will tax co-operatives' dividends and that an effort will be made to amend the Robinson-Patman law so as to define co-op dividends as rebates which are prohibited as a form of price discrimination. Another objective is reported to be an effort to prevent manufacturers from selling their products to consumer co-operative stores.

Printers' Ink observes that this is one more step in the battle of independents against developments in retail merchandising. When the department store was new retailers used every means at their disposal

to block that development; then the mail-order house became the object of their bitter opposition; and finally, in recent years, corporate chain stores have been the principal target of retailers' attacks. Now that the co-operatives begin to assume real significance in the merchandising picture, they will have to fight their battle for existence in legislative halls and in the forum of public opinion as well as in the economic arena.[1] The first step in planning that defense was made by national co-operative leaders in a strategy meeting in Chicago.[2]

The basic difficulty seems to be inherent in a capitalistic economy. Free enterprise, competition, and the profit motive have sometimes resulted in conditions against which consumers rebel. Unnecessary duplication of retail outlets results in larger overhead costs; competitive advertising and selling methods are not only expensive but often misleading; the desire for profit frequently results in restricted output or sale of low-quality merchandise. While it is possible for organizations of retail merchants to accomplish much in the way of eliminating undesirable selling methods, there is little or nothing they can do to prevent unnecessary duplication of facilities. Mr. H. F. Sinclair, President of the Consolidated Oil Corporation, says, "We have over-built service stations, wasted manpower, cross-hauled millions and millions of unnecessary miles and thrown away hundreds of millions of dollars in marketing expense. . . . " A survey made by his company showed that 35 per cent of the service stations then existing could serve the public adequately and conveniently. All of the waste which he cites he attributes to "our system of 'free enterprise' which we are fighting to maintain. . . . "[3]

On a question involving so many phases it is dangerous to be dogmatic, and difficult to draw conclusions. If the present method of marketing merchandise can be reformed it is quite clear that consumers' co-operation will hasten the process. Perhaps co-operation will become a yardstick in retail merchandising. Perhaps, as some enthusiastic co-operators believe, it will eventually become the prevailing system for retailing merchandise. European experience would suggest that the co-operative movement will become attached to our economic system, serving to speed reforms, acting as a constant threat in favor of consumers, but never wholly displacing the present system of private, competitive enterprise. European experience would also indicate that obstructionist tactics may retard but will fail to prevent the growth of

[1] *Printers' Ink*, September 17, 1943; *Business Week*, September 25, 1943; *Hardware Age*, October 14, 1943; *New York Times*, sec. 4, p. 8, July 9, 1944.

[2] *Ohio Farm Bureau News*, p. 22, December, 1943.

[3] SINCLAIR, H. F., *How the Oil Industry Can Contribute More to the Winning of the War*, Consolidated Oil Corporation, New York, March, 1943.

consumers' co-operatives. Those who believe with Mr. Janssen that the way for businessmen to meet this situation is to set their own house in order are right. The unanswered question is, Can they do it?

Advertisers and Consumers' Co-operatives. The consumers' co-operative movement constitutes a genuine threat to the business of advertising as at present carried on. Co-operators are not opposed to the use of advertising, but rather to its misuse. Obviously, there would be less advertising in a completely co-operative society. There would be no need for co-operative ventures to attempt to force a market for their products. This would be true for at least two reasons. Not only do they deal primarily in necessities, but the members as owners themselves decide the stock to be carried and the prices to be charged. As owners they would not supply themselves with things they did not want. Such advertising as might be used would be definitely factual, informative, and educational. The contrast between current advertising and that which might be expected from co-operatives is illustrated by the following announcement of muslin bed sheets and pillow cases offered for sale by Cooperative Distributors of New York City.[1]

> "Sheets and pillow cases that meet or exceed Federal Government Specifications DDD–S–281 for sheets and DDD–P–351 for pillow cases, except in the case of the crib sheets which, in the samples tested, were slightly below in several respects.
> Bleached cotton: first quality, plain weave.
> Average thread count: 74 × 68.
> Average weight: before washing, 4.7 oz. per square yard; after washing, 4.6 oz.
> Sizing: Not over 5% in the sheets; not over $3\frac{1}{2}$% in pillow cases.
> Average tensile strength: before laundering, 80 lbs. in the warp, 71 lbs. in the filling; after laundering, 74 lbs. in the warp, 69 lbs. in the filling.
> Average shrinkage per yard after one washing: $2\frac{1}{2}$ inches in the length, 1 inch in the width.
> Hems: sheets, 3 inches at one end and 1 inch at the other; pillow cases, 3 inches.
> Selvage: $\frac{9}{32}$ inch in sheets and $\frac{1}{2}$ inch in pillow cases.
> Stitches: plain machine, 14 to the inch.
> Torn size: $4\frac{1}{2}$ inches more than hemmed length; width: same."

Following these specifications a table of prices was given. A double bed sheet, 90 × 108, was priced at $1.57.

Prospective buyers of shaving cream were informed that it is com-

[1] *Consumers' Defender*, vol. 2, No. 1, March, 1936, p. 12. Further information concerning this organization may be secured by addressing Cooperative Distributors, Inc., 13 Astor Place, New York, N. Y.

posed of stearic acid, potassium palmitate, potassium laurate, potassium abietate, sodium silicate, glycerin derivative, and perfume. Shoe dressing was advertised as a nonpoisonous mixture of high-grade carnauba wax, ceresin wax, beeswax, neatsfoot oil, petroleum solvent, turpentine, and diphenylamine.

In addition to this type of informative advertising concerning products and services for sale, the co-operative movement devotes considerable energy to educational propaganda concerning the movement itself. It will be recalled that a common co-operative practice is to build up a reserve fund, part of which is used for educational purposes. The form which this takes is primarily issuance of bulletins, pamphlets, magazines, and books whose purpose is to acquaint nonmembers with the principles of co-operation. This is done, of course, in the belief that if consumers are informed concerning possibilities of this movement they will join it voluntarily and eagerly.

After a mysterious cancellation of contract by the broadcasting companies, the Cooperative League of the U. S. A. went on the air for a series of twelve weekly Sunday afternoon programs beginning in the fall of 1942. This was part of a national advertising or educational program, the central theme of which was the world of tomorrow. After stipulating that no disparaging comparisons would be made between co-operative stores and other types of retail stores, the co-op program concentrated on the positive characteristics of consumers' co-operation and requested listeners to write in for a booklet telling more about the movement. In 1943 the Cooperative League placed its entire advertising program in the hands of an established advertising agency. These two acts represent a departure from traditional consumers' co-operatives' policy and are being watched with interest and some concern by the business fraternity.

Participation in a co-operative is in itself educational. Members, as participating owners, learn a great deal about the methods of doing business. They become aware of the customary markup from wholesaler to retailer and from retailer to consumer; the ratios between operating costs and sales assume a new significance. There is a strong tendency in co-operative literature to belittle modern advertising and selling technique. All this has an effect on the co-operator beyond his actual participation in a local society. His skepticism of advertising is likely to grow and as the number of members of consumers' co-operatives increases, the effectiveness of much traditional advertising is almost certain to diminish.

This threat to advertising as at present carried on is ominous indeed. Much of it cannot stand in the face of rational, critical judgment.

Co-operators are going to realize that one reason their ratios of operating costs to sales are even lower than those for chain stores is because they are not under the necessity of spending such a large percentage of gross sales for advertising purposes. In the case of such commodities as patent medicines, whose advertising appropriations constitute a significant percentage of sales, co-operators are going to begin to ask what they receive in return. The answer will scarcely fortify the position of advertising. This threat can scarcely be met by superficial changes in advertising practice even if it were possible to effect such changes. Advertising may be honest but unnecessary. To the extent that this is true a considerable deflation would seem inevitable.

Small Businesses and Co-operatives. It is not without reason that 90 per cent of consumers' co-operatives in the United States are engaged in retail merchandising. It is in this field that a tremendous amount of waste occurs, due to unnecessary duplication. In 1932, for example, there were 156,671 gasoline filling stations, 111,594 of which were adjudged unnecessary in a survey made by the oil industry. It was concluded that this excess capacity resulted in an overinvestment of $1,000,000,000, causing an annual loss of $455,000,000. In terms which the consumer can understand, this means that the price of gasoline is 2½ cents higher per gallon than it would be otherwise.[1] A more recent investigation made by the oil industry in a community of 85,000 population revealed 16 bulk plants of which 13 could be closed, releasing 40 employees. There were 37 tank trucks in operation of which 9 were necessary. There were 315 retail filling stations, of which 187 were marked for temporary abandonment, releasing 103 employees. Another survey disclosed 12,600 filling stations in California of which 8,600 were unnecessary. By closing these unnecessary stations and dispensing with other facilities and personnel, it was estimated that $6,600,000 in rentals and interest could be saved every year.[2] The New York State Food Investigating Committee found one retail food store for every 250 persons in New York City. This meant the existence of four times as many stores as were needed.

There were 1,770,355 retail stores in the United States in 1939. These were divided among the several different types as shown in Table XXXI. A comparison of the figures for 1935 and 1939 indicates the continued trend towards a larger number of retail stores in almost every classification.

[1] *New York Times*, January 24, 1932. By 1939 the number of filling stations had increased to 241,858. [2] SINCLAIR, H. F., *How the Oil Industry Can Contribute More to the Winning of the War*, pp. 5, 7, 8.

Mr. E. A. Filene, himself engaged in retail merchandising, once estimated that from 75 to 90 per cent of the productive resources used in retail merchandising are wasted.

TABLE XXXI.—NUMBER OF RETAIL STORES IN THE UNITED STATES, BY MAJOR BUSINESS GROUPS, 1939 AND 1935[1]

Kind of Business	*Number of Stores*	
	1939	1935
Food group	560,549	532,010
General stores (with food)	39,688	66,701
General merchandise group	50,267	44,651
Apparel group	106,959	95,968
Furniture-household-radio group	52,827	45,215
Automotive group	60,132	50,459
Filling stations	241,858	197,568
Lumber-building-hardware group	79,313	73,186
Eating and drinking places	305,386	251,473
Drug stores	57,903	56,697
Other stores	215,473	173,790
Totals	1,770,355	1,587,718

Casual observers in almost any community will substantiate the conclusion to which these figures lead. In a village composed of 350 families one would probably find 6 retail grocery stores, while another town composed of 700 families would probably divide its patronage among 12 such stores.

Statistics supply the facts and support the conclusion. But what is the reason? The answer is to be found in the system of free enterprise which permits any individual who by some means can secure the necessary capital to open a retail store no matter whether or not there is a community need for it. A supplementary reason is to be found in the small amount of capital required to undertake a new business. This tendency toward duplication of retail outlets is unconsciously encouraged by the system of offering for sale branded or trade-marked merchandise. Each manufacturer seeks an exclusive outlet for his products. As a result six different brands of gasoline will probably be sold by the six different service stations nearest together. While this system of free enterprise has its virtues it also has its defects. One of the defects is the large number of failures among small retail merchants. These small businesses contribute far more than their normal proportion to the large

[1] United States Department of Commerce, Sixteenth Census of the United States, 1940; Census of Business, vol. 1, *Retail Trade, 1939,* Part 3, p. 5, United States Government Printing Office, Washington, 1941.

number of annual business failures. In the face of such overexpansion a high percentage of failures is inevitable. Small, independently owned stores have been conducting a life-and-death struggle with the chain-store octopus and now find themselves faced with another ominous threat.

Exactly how ominous is this threat? Leaders in the co-operative movement contend that co-operation offers a way out for the small-business man. Retail merchants are told that the way to meet the situation is to co-operate with the co-operative movement by converting their stores into co-operative enterprises. That this is a real possibility is attested by the fact that some retail stores have been so converted. Obviously, this is a more socially desirable procedure than for a co-operative to add duplication to duplication by opening still another retail outlet. But when, in a community composed of 350 families, one of the six groceries is converted into a co-operative, what will happen to the other five groceries which attempt to continue as private enterprises? If every family in the community should become affiliated with the co-operative store, a part but not all of the personnel and equipment formerly used would be necessary to supply adequate service. One or two large storerooms would displace the half dozen previously used. Working hours, notoriously long, could be reduced. Secondary effects would be felt among existing wholesale supply houses. A smaller number of co-operative wholesalers could supply adequate service.

The period of transition leading to such a completely co-operative community would necessarily be long. The changes envisaged would be gradual. Not every family could be expected to affiliate with the co-operative enterprise. Much of the business transacted by privately owned, independent stores depends on a loyal clientele of community friends who confine their purchases to a particular store for other than economic reasons. This no doubt accounts for the fact that, as American experience has shown, the co-operative store is a much more formidable threat to the chain store than to the independent. There are those who contend that the co-operative movement is the small-business man's best means of meeting the chain-store threat.

Limitations of the Co-operative Movement

Bigness and Real Democracy Are Incompatible. The genius of co-operatives lies in small, local groups characterized by democratic ownership and control. Breakdown of the true co-operative principle has been noted in the cases of insurance and of housing, where large numbers or large capital are essential. It is difficult to envisage successful operation by voluntary consumers' co-operatives of far-flung industries requiring

large amounts of capital investment. Certainly it would take a long time for consumers to raise the necessary capital to acquire ownership of such enterprises as railroads, telephones, telegraph lines, and steel mills. By their very size and geographic dispersion democratic control would be difficult if not impossible. Yet consumer control, in consumer interest, of these types of enterprise would be needed as much as in retail merchandising.

In the opinion of leading English co-operators the solution is to be found in what they call compulsory co-operation—in other words, an intelligent state socialism which would obligate consumers as citizens to co-operate in the control of such enterprises. The experience of Sweden is illustrative. A strong consumers' co-operative movement is supplemented by a socialist government whose nominal head is the king.

Political Impotence. A second limitation of the consumers' co-operative movement as it is developing in the United States is the political impotence of the several thousand local co-operative groups. These are organized primarily as small, economic, fairly independent units with little cohesiveness. It is true that many of them are affiliated with co-operative wholesales which in turn are affiliated with the Cooperative League, but probably the greater proportion of them are quite independent units. As such they have no articulate voice in local, state, or national politics. Recent experience with price control and rationing has demonstrated once more the notorious neglect of organized consumers. The apparent solution for this difficulty is affiliation with some political party whose aims and ideals most nearly coincide with those of the co-operative movement.

American Tradition. A third limitation to rapid expansion of the co-operative movement is the background of American tradition. The United States today is the last large stronghold of the philosophy of rugged individualism. There are evidences that this philosophy is breaking down, but only gradually. There is still a deeply rooted conviction in the minds of millions of Americans that the fundamental economic virtues are self-interest, competition, free enterprise, and the profit motive. In England, the birthplace of that philosophy, a century of co-operative growth has left its mark but has by no means displaced the system of privately owned competitive business.

In the United States a reawakened church has shown an increasing tendency to give attention to the fundamental inconsistencies between Christianity and these long-cherished doctrines. The speed with which the church succeeds in this venture will measure to a large degree the resisting power of these traditions.

A Logical Basis for Economic Organization. Since the ultimate purpose of any economic system is to provide consumers with goods and services, a system whereby consumers themselves perform that function is at least as logical as any other. Under the present system consumers control productive processes in *theory;* under the co-operative system consumers control productive processes in *fact.*

Co-operation Eliminates Competitive Evils. Preceding chapters have called attention to consumers' complaints concerning such competitive results as adulteration, misrepresentation, bad advertising, price wars, and unbalanced, misdirected production. These are almost entirely the result of ineffective consumer control. Consumers' co-operative enterprises tend to eliminate the problem of adulteration. This is true because consumer-owners themselves determine the standard of quality. Their motivation is to provide themselves with good merchandise rather than to make a profit. For the same reason, the practice of misrepresentation would disappear. In place of one group, known as producers, presenting its wares to another group, known as consumers, the co-operative scheme identifies the interests of consumers with those of producers, since both groups are identical. While advertising would not be displaced entirely, it would be reduced considerably and would assume altogether different forms. Price wars are an outcome of competition. Since co-operation supplants competition, price wars, with their consequent effects on quality and wages of labor, would largely disappear. The members of consumers' co-operatives know that any savings resulting from good management will be returned to them in the form of patronage dividends. The evils of unbalanced and misdirected production which result from free enterprise and the profit motive would be corrected. Consumers exercising actual control would not undertake to supply themselves with large quantities of unwanted merchandise. Their terest is primarily that of securing a steady flow of necessities rather an an intermittent flow of unnecessary goods.

Co-operation Is Evolutionary and Democratic. Perhaps one of the most stinctive features of the co-operative movement is its ability to develop d thrive within the framework of another type of economic system. gland, Denmark, Sweden, and Norway could all be described, and curately, as capitalist countries. Yet they are also the four countries which the co-operative movement has reached its highest stage of velopment.

Another remarkable feature of this form of economic organization the power which it puts into the hands of consumers to protect and

promote their interests as consumers. There is no need, beyond that of a necessary enabling act, to seek by legislation to protect their interests. Insofar as consumers supply themselves there is no necessity for demanding legal standards of purity for food; laws regarding quality of other products would be less essential if not wholly unnecessary; and legal restrictions on monopoly would be less effective than direct competition. The experience of Swedish co-operatives in manufacturing electric light bulbs in competition with a firmly entrenched monopoly is an example. Not only are consumers spared the struggle of attempting to place such laws on the statute books, but it follows naturally that they are not harassed with a problem of law enforcement. It is literally a case of consumers taking the law into their own hands.

A commonly cited paradox is our failure to parallel political democracy with democracy in industry. Our economic system is obviously controlled by a small group of men made powerful by the possession of tremendous wealth. Estimates as to the number of persons who own and control the United States vary. The late Mr. George F. Baker testified before the Pujo Investigating Committee in 1913 that no important business could be financed in the United States without approval of himself, Mr. Morgan, or Mr. Rockefeller. Former Ambassador Gerard, as reported in 1930, believed that sixty-four people, not including the President or any other political officials, controlled the economic life of the nation.[1] Mr. Ferdinand Lundberg contends that control lies in the hands of sixty families.[2] For generations workers have sought by means of legislation and force to secure some voice in the control of industry. Without political struggle or revolution the consumers' co-operative movement has developed quietly within the framework of the present system and has laid the groundwork for a possible ultimate democratic control of production by consumers. There is another advantage. Many persons who find themselves dissatisfied with present conditions are yet too conservative to affiliate themselves with a socialist, communist, or other radical political movement. Such conservatism may spring from an honest conviction that such efforts are futile, or (and this is more likely) from a fear of popular disapproval of anything called radical. The power of this fear may be illustrated by the growing tendency of opponents to describe the co-operative movement by the dreaded word communism. There can be no doubt that such tactics will succeed with some people; but for the most part the co-operative movement has not yet fallen under the ban of radicalism. As a result it has drawn many recruits from conservative and low-income groups.

[1] *New York Times*, August 24, 1930. [2] LUNDBERG, Ferdinand, *America's Sixty Families*, The Vanguard Press, New York, 1937.

Co-operative Abundance. Perhaps the weakest link in the capitalist chain of theory is its dependence on scarcity. The theory of value holds that prices will be higher as supply diminishes. Individuals as producers concerned with their self-interest thus find it possible not infrequently to promote their own interest by limiting supply, securing thereby higher prices and expanding their profit. For generations American consumers have tolerated an economy of scarcity in the presence of physical abundance. With governmental aid manufacturers have secured restrictive tariffs whose effect has been to limit supply and raise prices to American consumers. Under the aegis of tariff protection monopoly has developed, to exploit the home market (consumers) by limiting supply so as to raise prices. Residents of seaport towns have grown callous watching fruit shippers dump portions of their shipments into harbors, while consumers in inland cities are not unaccustomed to the practice of shippers destroying a part of vegetable receipts so as to secure prices which will yield attractive profits.

Diametrically opposed to the economy of scarcity is the idea that consumer welfare will be promoted by the production of abundant supplies of things which people need. In order to eliminate the conflict of interests which now characterizes relations of producers and consumers, the consumers' co-operative movement places the consumers themselves in the role of producers whose first concern is to supply themselves with an abundance of the goods they want. The idea of scarcity is alien to co-operative philosophy. The term abundance is here used in a relative sense. By its very nature, and unlike many political movements, the co-operative movement keeps its feet on the ground. Or perhaps it should be said that the co-operative operation of business keeps its feet on the ground. Co-operators have no illusions concerning a Utopian abundance. They know from experience that whatever wealth they get will be earned by expenditure of human energy. But they also know by experience that greater relative abundance of wealth can be secured under a system which encourages rather than restricts the creation of new wealth.

Future of the Co-operative Movement in the United States

The Consumers' Co-operative Movement Has Definitely Become an Integral Part of the American Economic System. Its phenomenal growth during the past decade represents the flowering of a movement planted a generation before. While expansion cannot be expected to continue at the rapid rate characteristic of recent years, there can be no doubt that it will continue. There are a number of reasons leading to this conclusion. Some of these have already been given. The necessary enabling legisla-

tion has been quite generally enacted, although attempts to amend or repeal these laws will grow in number and intensity. Its success, as well as the attitude of government, will depend largely on the political power of co-operatives as compared with that of their opponents.

Increasingly consumers are becoming aware that the co-operative movement has proved itself as a way toward consumer welfare. The tendency toward monopoly, always present, serves as a stimulus to consumers to organize themselves co-operatively. Consumers will come to place more reliance upon co-operation and less on legislation to protect their interests. This is illustrated by the venture of Ohio farmers in setting out to provide themselves with electricity co-operatively. Efforts to secure adequate service at reasonable rates, having failed of achievement by law, were sought by co-operation. The success of Swedish co-operators battling monopoly may point the way for American consumers.

There is no indication that prevalent wastes in advertising and retail marketing will be reduced. Appropriations for advertising and selling increase rather than diminish. The nature of advertising appeals shows but little, if any, improvement. Unnecessary duplication of retail outlets, particularly food stores and filling stations, continues. Even where marketing costs are reduced by chain organizations, consumers are without adequate protection against misrepresentation and poor-quality merchandise. A rising price level with the threat of increasing inflation hangs like a sword of Damocles over consumers' heads. As their knowledge of consumer co-operation grows they will turn to it to expand their limited incomes. The Committee on Distribution of The Twentieth Century Fund recommends "the further organization of consumer cooperatives and consumers' group buying agencies as one way of developing consumer knowledge for the improvement of marketing."[1]

The philosophy of rugged individualism is rapidly giving way to a realization of the need for co-operative living. The United States as a nation has passed from immaturity to maturity. This is not to suggest that consumers' co-operation will slip into the place of capitalism. Rather, a steady growth can be expected which will result in an increasingly large proportion of co-operatively supplied goods and services. A century of growth in European countries has carried co-operatives to the point where they supply from a third to a half of consumers' needs. Perhaps this experience may be duplicated in the United States.

Co-operation as a Movement. The phrase "co-operative movement" has been used frequently. Possibly the strongest reason for believing co-operatives will expand is found in the implications of the word

[1] STEWART, Paul, and DEWHURST, J. Frederic, *Does Distribution Cost Too Much?*, pp. 352, 353.

"movement." To real co-operators the co-operative movement is more than a mere means of supplying economic goods. Co-operation becomes a means of reform and to that extent an end in itself. Co-operators become imbued with a missionary zeal. The very act of co-operating is educational in business and government and in democracy. This helps to explain the increasing interest of the church in co-operatives. The National Catholic Rural Life Conference and the Universalist Church have endorsed consumers' co-operatives as an application of Christian principles to the economic order.[1] The movement is spreading rapidly on college campuses. A new interest in co-operation may be detected on the part of organized labor. If the interests of workers, colleges, church, and state are combined, this democratic means of economic reform will certainly assume an increasingly significant role in American economic life.

Increasing attention is being given to the possible role of co-operatives in postwar relief and reconstruction. A Committee on International Cooperative Reconstruction of the Cooperative League of the United States of America was created in 1942 and has offered its services to the director of Foreign Relief and Rehabilitation Operations. In doing so it emphasized the desirability of making use of existing co-operatives because they carry on business for the purpose of service, they have extensive experience in local, national, and international commerce, they have warehouse facilities at their disposal, and they represent no political, racial, or sectarian group; rather they consist of all kinds of people and exclude no one. Co-operatives were widely used for relief and rehabilitation after World War I in France, Italy, and the Netherlands. In the midst of World War II the Swedish government was using the over-seas agencies of the Swedish co-operative wholesale for the importation of goods, both for co-operatives and for private businesses. It seems quite likely that consumers' co-operatives will perform signal service in the task of international reconstruction at the end of World War II.[2]

Summary

The American labor movement, developing along craft lines, has emphasized workers' interests as producers instead of their interests as consumers—this in spite of the fact that scarcely more than one third of all consumers are gainfully employed and hardly more than 25 per cent of all eligible workers belong to independent unions. Sporadic

[1] *Monthly Labor Review*, vol. 50, p. 657.

[2] *Business Week*, April 10, 1943, p. 40; also a press release from the Committee on International Cooperative Reconstruction, the Cooperative League of the U. S. A., New York.

efforts of trade unions to organize consumers' co-operatives have usually failed as a result of violating co-operative principles. When the simple truth is realized, that workers' interests as consumers precede their interests as producers, the American labor movement may be expected to embrace the co-operative movement.

Until recently businessmen have regarded the co-operative movement with tolerant amusement but now it looms as a threat to the prevailing system of merchandising. It is doubtful whether businessmen can effect any fundamental change which will meet consumers' criticisms. Perhaps co-operation will become a merchandising yardstick.

Consumers' co-operation does not object to advertising, but to the abuse of advertising. Not only would co-operators use less advertising; its form and character would differ. The co-operative threat to advertising as practiced is serious indeed.

Merchandising is overcrowded, as a result of free enterprise and small capital requirements. Tremendous waste results and is one factor in the growth of co-operatives. Competition is keen and even ruthless; business failures are numerous. Co-operators contend that co-operation is the hope rather than the doom of independent retail merchants.

The co-operative movement is no panacea. It has its limitations. These include the difficulty, if not impossibility, of maintaining democratic control in large ventures, the political inarticulateness of co-operators, and the strong American belief in individualism and competition.

Economically the co-operative movement is sound. Experience has proved its practicability. Theoretically consumers should control the economic system, yet co-operation alone makes consumer control a reality. It eliminates competitive evils, is evolutionary and democratic, and builds on an abundance of wealth rather than on scarcity. The consumers' co-operative movement has definitely become an integral part of the American economic system and may be expected to expand in importance.

QUESTIONS FOR DISCUSSION

1. Compare the theory of collective bargaining with the theory of the consumers' co-operative movement.
2. Are the labor movement and the consumers' co-operative movement mutually exclusive?
3. If your father is a businessman is he familiar with consumers' co-operation? If so, what is his attitude? What is your own attitude?
4. Do you think Chambers of Commerce can forestall the development of an American consumers' co-operative movement by improving the prevailing marketing system?
5. Compare the efficiency of co-operatives and chain stores.

6. If you have no relative or friend associated with an advertising agency assume that you are. What attitude do you think you or your relative or friend would take toward consumers' co-operation? Would such an attitude be rational?
7. What would be your attitude toward the beginning or the expansion of a consumers' co-operative movement in your community?
8. Do you think co-operatives should participate in politics?
9. Should the church take any cognizance, either favorable or unfavorable, of the consumers' co-operative movement? If such a question arises in your denomination how will you vote?
10. Is consumers' co-operation economically sound?

PROBLEMS AND PROJECTS

1. Interview retail merchants, including operators of filling stations, in your vicinity, to ascertain their knowledge of and reaction to the consumers' co-operative movement.

2. Make a study of retail distribution in your community. How many stores of various kinds are there per family? How much unnecessary duplication do you find? Estimate the waste, in terms of dollars.

3. If there is a consumers' co-operative near by write a report on its history. Check its organization and operation with Rochdale principles and methods.

4. Secure from the Secretary of State of each state copies of laws pertaining to co-operatives and credit unions. Digest and analyze these laws, showing which states have none and which have the best laws.

5. Compare the advertising in a typical periodical with that in a co-operative publication. On the basis of your comparison make an estimate of the extent to which advertising would be reduced in volume if all economic activity were on a co-operative basis. Make a similar estimate, assuming that the co-operative movement, as in European countries, will eventually embrace about one third of the population.

6. Examine the files of *Business Week*, or *Printers' Ink*, or *The Nation's Business*, to ascertain the attitude toward consumers' co-operation.

7. Assume that you are going to organize a co-operative on your campus to supply some needed commodity or service. Write to the Bureau of Labor Statistics in Washington for Bulletin 665.

8. Review one of the following books: Bolles, J. K., *The People's Business;* Childs, Marquis, *Sweden: The Middle Way;* Cowling, Ellis, *Cooperatives in the United States;* Warbasse, J. P., *Cooperative Democracy* (1942).

9. Interview labor union officials in your vicinity to ascertain their reaction to the consumers' co-operative movement. Supplement this report with a proposed co-operative program for labor leaders.

10. Prepare a brief history of the Cooperative League of the United States of America, emphasizing the part of this organization in the co-operative movement.

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Buying Protection: Principles of Insurance

What Is Insurance?

Insurance Is Protection. The technique of consumption includes a knowledge of how to buy intangibles as well as tangibles. Perhaps most important among these intangibles is protection against certain hazards, many of which result from our modern manner of living. The term which describes and covers this protection is "insurance," which may be defined as that social device for making accumulations to meet uncertain losses resulting from damage to, or destruction of, life or economic wealth, which is carried out by transferring the risks of many persons to one person, or to a group operating as a company, by means of a contract.[1]

In buying insurance the tangible thing one secures is the contract which sets forth in detail the obligations and benefits falling upon or accruing to the parties involved. As is true of many other purchases the consumer makes, he usually knows much less about the thing he is buying in an insurance contract than does the seller. The seller not only knows the exact meaning of every term, both technically and legally, but he also can measure the profit or loss anticipated and consequently has a definite standard by which to determine his commitments. The individual consumer buyer, on the other hand, cannot even understand the terms used by insurance salesmen; he knows little or nothing about the law of insurance; and he has no definite standard of profit or loss to guide him in his buying. In short, the seller is a specialist while the buyer is an amateur.

Since the contract is the only tangible thing passing from the seller to the buyer of protection, it is all the more essential that the buyer inform himself as to its provisions, their exact meaning, the integrity and financial responsibility of the seller, and the adequacy of that particular contract to protect him if the event insured against occurs.

[1] Adapted from Huebner, S. S., *Life Insurance,* p. 3, D. Appleton-Century Company, New York, 1935, and Huebner, *Property Insurance,* p. 3, D. Appleton-Century Company, 1938. For the technical phases of the subject I have drawn on Huebner's *Life Insurance.*

How Much Insurance Should One Carry? There are so many individual variations, such as one's age, health, income, and number of dependents, that no definite rule can be given as to the proper amount of insurance. Unfortunately, few consumers can afford to buy as much protection as they need and still maintain a desired plane of living. But the ideal toward which they should aim is to buy that amount of health and accident protection which will maintain income during incapacitation; that amount of life insurance which will yield an income sufficient to enable dependents to maintain their present plane of living;[1] an annuity which, supplemented by the cash value of insurance at age sixty-five, will provide for maintenance of the accustomed plane of living after retirement; and an amount of property insurance which will cover substantially any loss caused by damage to or destruction of such acquired wealth as personal effects, furniture, automobile, and dwelling.

Generally speaking, women should carry little or no life insurance. This is because the purpose of life insurance is to protect the dependents of the one who is responsible for their economic welfare. If a married man with three children dies his earning power must be replaced by insurance; if the mother dies there is no loss of income, except in a few cases. Consequently all the premium money which a family can spare should be used to purchase insurance on the life of the one earning the family income. If the mother is contributing to the family income she is justified in carrying a proportionate amount of insurance, otherwise a $1,000 life policy designed to cover last illness and burial expenses should be regarded as the usual maximum.

What Kinds of Insurance Should One Carry? In plainer language, against what hazards should one buy protection? In general, against those events which are certain or most likely to befall an individual, impairing or terminating earning power and damaging or destroying accumulated wealth. Economically a human life has a capital value equal to the capitalized value of its net earning power, at an assumed rate of interest. Thus the man with a net income for dependents of $125 a month represents a capital sum, at 3 per cent interest, of $50,000, that being the amount which, invested at 3 per cent, would yield them $125 a month.

The one certain event is death. So certain is that fateful end, in fact, that the only uncertainty is when it will occur. Between ages eighteen

[1] This may be ascertained by deducting from the total amount of family expenses all expenses incident to the insured which will cease at his death, such as insurance premiums, his own living costs, and personal expenses. A family budget will facilitate this calculation. For example, a man earning $250 a month, with three dependents, should probably provide an insurance estate large enough to yield approximately $125 a month.

and sixty-five premature death cuts off anticipated earning power and it is against that risk that one should protect dependents.

A very likely event is nonfatal illness which temporarily or permanently eliminates or reduces income-earning power. Moreover, not only is income stopped or reduced, but medical expenses soar. Through wiser consuming and observance of health laws one may enjoy good health, but sane and careful living is no certain assurance of health. Living, as we do, in crowds, the risk of ill health is magnified, and modern production methods are responsible for an increasing amount of occupational disease. The chance that one will pass through this world without a single impairment of health is small. For that reason one should buy protection for oneself and for one's dependents against that hazard.

The modern machine has great power to produce wealth but it also has great power to maim and destroy the humans who made it and use it. Speed in transportation has reduced time and space, but it has also brought untimely death to thousands and annually claims or threatens thousands more. The child at play, the office worker en route home, the manual worker at his task, and the housewife in her mechanized kitchen are constantly exposed to the possibility of physical impairment or death through accident. As in the case of illness, not only is income suddenly stopped but medical expenses mount and the family unprepared to meet this situation may see its savings disappear and debt take their place. One may gamble if he wishes and may win. But if he loses the loss will be so great that as a wise consumer he should protect himself and dependents against the hazard of accidents.

If one escapes death, illness, and accident, and survives to a ripe old age a new hazard appears in the danger of dependency. The possibility that one will fall victim to this hazard is indicated by the estimate that of 8,600,000 persons over 65 years of age in the United States in 1941, 5,218,000 were dependent. Of that number 2,632,000 were dependent on relatives and friends, and 2,586,000 were supported by public or private social agencies. If inadequate provision has been made for this contingency the later years of life are clouded by the necessity of looking to one's relatives or to society for subsistence. In the optimism of youth it is easy to assume that one's earning power will enable provision for old age. But with the exception of a comparatively few professional men and women, earning power declines with advancing years and, depending upon variations in occupations and health, completely stops at various ages from fifty on. To be realistic one should anticipate retirement at age sixty-five. And unless a definite investment program in the form of annuity purchase is undertaken when income permits, the chances are

approximately fifty-fifty that the years which should bring fullness of life will bring dependency instead.

In addition to these personal risks there is the ever-present possibility that wealth acquired through the years may be destroyed, damaged, or lost as a result of fire, storm, flood, collision, war, theft, or loss. Any one of these calamities may befall the wealth we cherish. Regardless of one's position in the income group, everyone possesses certain personal effects such as clothing, jewelry, and trinkets; and each family has accumulated furniture, linens, dishes, tableware, pictures, and books. While for most of us these things are replaceable it would be financially impossible to restock the home all at once, in event of loss. If the family owns the house which it converts into a home, it daily faces the risk of having that house destroyed or damaged by fire or wind or water. Unless provision is made to meet that hazard if it comes, it is more likely than not that the house cannot be replaced or repaired.

If the family income is large enough to permit saving and the saving is in addition to or in lieu of tangible wealth owned, it will be in the form of what are loosely called securities. These include the bank passbook, building and loan association passbook, postal savings certificates, insurance policies, bonds, and shares of stock. Kept in the home, these evidences of wealth are subject to loss or destruction by theft, fire, etc., but in most cases these hazards can be guarded against most economically by storing them in a safe deposit box in a bank vault. The usual charge for a personal-size box is $2.00 a year.

With increasing ownership of automobiles, owners are incurring new risks. In addition to the hazards of fire, theft, and collision resulting in damage to or destruction of the car, the owner incurs legal liability for damage to or destruction of the lives and property of others. If this risk is assumed individually and an accident occurs the owner may find himself faced with a court judgment for thousands of dollars. If he does not own enough wealth to meet the judgment it becomes a first lien upon any wealth he may subsequently acquire. Under the Ohio law his license to operate a car will be revoked. Because of the increasing probability of accident and of the size of the liability assumed, the owner of an automobile who fails to buy insurance protection for himself and his dependents is doubly improvident and unwise.

Principles of Insurance

How Should One Meet These Hazards? Some people take a chance that none of the events above mentioned, except death, will befall them. In the Near East people customarily wear a blue bead to ward off the evil eye. But neither there nor here will the blue bead, or the rabbit foot,

or any other "charm" have any effect; the fact is that these calamities do occur. And for the improvident they are doubly calamitous. Death is the end which comes to all, and the man who awaits its uncertain coming without making such provision as he can afford for his dependents is not only selfish but thoughtless of those who are dependent upon him.

Another method of meeting these risks is to attempt to accumulate a liquid store of wealth, usually called savings, which may be drawn upon if and when any of the events occur. If none of them happens, this individualist can leave his savings to his dependents when he dies. But three fatal defects of this method are obvious. In the first place, 75 per cent or more of the income receivers in this country receive such small incomes that they cannot possibly lay aside enough surplus to provide any substantial benefit. Moreover, in case of those whose incomes make this method of self-insurance possible, there are the constant uncertainties to life itself, and to health. Any premature stoppage of income obviously will render impossible the accumulation of the desired surplus. A third defect is the patent inability of the individual to invest his savings wisely so as to yield maximum income and insure safety of the principal.

A third, and much wiser method, is to co-operate with others who face the same risks. By pooling the limited surpluses of members of the group, enough can be secured to reimburse effectively the unfortunate few upon whom the evil eye does fall. This method substitutes a small, certain loss (the premium) for a larger, uncertain loss. In so doing it not only enables the individual to meet the financial loss if and when the event occurs, but it also reduces or eliminates the worry caused by uncertainty incident to either of the other two methods. This is the insurance method.

A simple illustration of its use to meet the two most common and greatest hazards, death and fire, will clarify its operation.

Assume that 1,000 young men, age 21, graduating from college next June wish to assure their parents repayment of $1,000 advanced for college expenses in case they should die prematurely. Information available in the form of mortality statistics makes it clear that only eight of the thousand are likely to die during any one of the next five years. To protect their parents against the hazard of their premature death during the five-year period when they expect to pay off the loan, each man pays in $8.28 each year. This fund of $8,280 is invested to yield a rate of interest which, added to the principal, and improved by subsequent premiums, will be sufficient to meet expenses of administration and each claim falling due. Thus each of these men has substituted a

small, certain loss ($8.28 a year) for a larger, uncertain loss ($1,000) to his parents. The simplicity of this illustration of course detracts from its accuracy, but the general principles shown are those upon which life insurance is based. Merely by increasing the number from 1,000 to 100,000 so the law of probability would apply more dependably, this simple example would be typically accurate.

Now let us suppose that the parents of each of these young men own a house valued at $10,000, that the houses are substantially similar, and that the annual fire loss for the group averages 0.5 per cent, or $50 per house. The known loss for the group will be $50,000 during the year. In other words, 5 of the houses will burn. But since no one knows which 5 of the 1,000 will burn all can protect themselves by paying into a common fund $50 apiece. By this means $50,000 is accumulated to reimburse the 5 upon whom the fire loss falls. In a sense insurance is thus seen to be a communistic means of sharing risk and loss. But what did the 995 whose houses remained intact get for their $50 expenditure? Each of them got just what he contracted for—the assurance that if his house had been destroyed his net loss would have been reduced from $10,000 to $50. In the same way every buyer of insurance of whatever kind gets exactly what he buys, which is the assurance that if the undesired contingency does befall he will be reimbursed out of the payments made by those who are insured. Properly regarded, one never loses when buying sound insurance, for what is bought is protection, which is delivered day by day and hour by hour.

Principles of Sound Insurance. There are certain basic principles underlying the operation of sound insurance. First of the four chief principles is that the number of objects insured must be large enough for the law of large numbers to apply. This law has been alluded to in the illustrations just given. We may predict what will happen in a group numbering 1,000 with greater accuracy than in a group of 100. By the same token we may predict what will happen in a group numbering 100,000 with still greater accuracy and on the basis of that prediction calculate accurately the annual premium charge needed to yield the sum necessary to reimburse the claimants.

A second general rule underlying all sound insurance is that the person or persons designated in the contract to receive the indemnity provided must be ones who would suffer a financial loss if the event insured against should occur. In underwriting parlance, the beneficiary must have an insurable interest in the life or property insured. In cases of health and accident insurance the insured has an insurable interest; in the case of life insurance any dependent possesses an insurable interest in the life of the insured; in the case of property insurance the owner

enjoys an insurable interest in the property. With the development of insurance the concept of insurable interest has broadened. Not only dependents but also creditors, business partners or affiliates, and employers are recognized as standing to suffer financial loss if the life or property insured is destroyed. The reason for limiting beneficiaries to persons possessing insurable interest is to avoid writing insurance contracts in favor of anyone who would gain more by having the life or property destroyed than by having it preserved.

Closely related to the second principle is the general rule that the amount of indemnity must not exceed the loss incurred by the happening of the event insured against. Obviously, if a $10,000 house were insured against fire loss for $20,000 the owner would gain if a fire occurred. In fact the gain would be so material that in a moment of weakness he might himself bring about the very loss insured against. How can this principle be applied when insuring human lives? In case of insurance to cover loss of health temporarily or permanently it is reasonably simple to limit the indemnity to a portion of the insured's earning power; otherwise he might find it gainful to develop chronic illness. In case of non-maiming accidents the same rule is applicable. But who shall say how much reimbursement is justified for the loss of the right eye or left foot? And still more complicated is the combination of the right eye *and* left foot. While an individual contract might be written in accordance with the hazards of one's occupation or the importance of certain members, such as the fingers of a pianist, the element of insurance would give way to the practice of betting, and the cost would be prohibitive for most persons. As a consequence this problem is usually resolved by setting an arbitrary indemnity for the loss or impairment of certain parts of the body.

How much is a human life worth? The economic answer to this question, as has been suggested, is the capitalized net income attributable to that life. Thus a man who provides to his dependents a net income of $1,500 a year could and should be insured for at least $50,000.[1] But how much more could be written with due regard for the principle under consideration? The non-economic value of human life is immeasurable. In a recent year at least 50 persons in the United States carried over $1,000,000 of insurance, each, on their lives; one of them, Pierre du Pont,

[1] It is evident that a man earning a total income of only $3,000 a year cannot afford a $50,000 insurance estate. He can, however, assure his widow a sufficient income to maintain her during her lifetime and can assure his children an adequate income until their maturity by judicious use of term or decreasing-term contracts, popularly known as family-income policies, when added to whole-life contracts, and by having the principal sum used to purchase annuities. At the end of the annuity periods there will, of course, be no remaining principal.

carried $7,000,000 worth in one year, none of which was business insurance. It may be asserted safely that no one company wrote the entire coverage for the valuable Mr. du Pont. The rule which most companies follow is to limit the amount on any one life. One company has a scale which limits the coverage on a single life according to age. A man between ages 20 and 24 is restricted to $200,000, while another company has a flat limit of $500,000. All policies in excess of these limits are syndicated or reinsured, so as to spread the risk.

A fourth basic principle of sound insurance is that it must be possible to determine when the event insured against has occurred. This raises no problem in the case of life insurance, for death is certified by public officials. Nor does it give rise to any great difficulty in the case of property insurance, for physical destruction or damage is evident. There is room for doubt in cases of accident and health insurance, since the judgment of a physician is involved in determining the extent and duration of disability, but the problem is not difficult. An example of uncertainty is afforded in the case of insurance against unemployment, but, generally speaking, the types of insurance which one should carry comply with this general principle.

Insurance Is Protection, Not Investment. Even more fundamental than the four principles just discussed is the principle that all insurance is basically protection against hazards. In buying an insurance policy of any kind the purchaser is buying protection from the hazard named in the contract. This is most evident when insuring property. A policy insuring protection against loss by fire cannot prevent destruction of the property, although the fire prevention program of underwriters may reduce the number of fires and the annual loss attributable to them, but it can reimburse the owner for his personal loss by collecting $50 from each of the 1,000 policyholders and turning a portion of that common fund over to him. The $50 which each of the owners pays will give protection for only a limited period, however, for total collections are just sufficient to meet total claims, including, of course, administrative expenses for twelve months. It therefore becomes necessary for the owner to pay out another $50 for the second year, another $50 the third year, and so indefinitely as long as he wants protection. At the end of 200 years the amount paid for protection would equal the present capital value of the property. This type of insurance is described as a term policy. It provides protection at the lowest possible rate, based on actual cost in the form of claims paid each year. Unlike a life, there is no certain end to the property; it grows old and needs repair but there is no certain, sudden end to it. In fact it *may* grow more valuable because of its age. Consequently no fund of $10,000 need be built up to reimburse the owner of

each of the 1,000 houses; as long as the average number of fires remains the same an annual charge of $50 will yield the necessary $50,000 to reimburse the 5 owners on whom the fire loss falls. Stated more concisely, the annual premium covers the cost, because the event insured against may never occur, and is therefore a level (uniform) annual charge which usually does not increase. Notice also that the annual premium does not decrease, nor does the contract call for the return of any premiums paid, either singly or in a lump. For $50 every twelve months the owner gets exactly what he buys, protection, at the lowest possible price.

The protective feature of insurance is further illustrated and emphasized in the cases of health and accident coverage. On the basis of public health records and accident reports it is possible to predict with a high degree of accuracy how many in a group of 100,000 people will be sick or injured during any year and how long they will be incapacitated. Arbitrary indemnities can then be set up, such as $25 a week for a maximum of 104 weeks total disability, or $1,000 for the loss of the left hand, or $5,000 for death if the result of a certain kind of accident, with almost perfect assurance that a $40 annual premium will yield a common fund large enough to pay all claims and cover expenses of administration. Like fire rates, these premiums are level annual term charges for protection against the hazard named in the contract, because the event or events insured against may never occur. If the insured lives through the year in good health and uninjured he is happy. The insurance company did not keep him well and safe, nor could it guarantee health and escape from injury; but it could and did guarantee him that *if* sickness or accident had befallen him he would have received financial aid as stated in the contract to reimburse him for lost salary and medical expenses. The $40 which he paid for protection went to reimburse the unfortunate men on whom the loss did fall, and for administrative costs.

Health and accident rates resemble fire rates in another respect. As a building grows old, if it deteriorates and becomes a fire trap the rates go up and finally the company refuses further insurance when the risk is so great that the premium would be prohibitive. While it is customary for health and accident rates to remain uniform, making allowance of course for differences in occupation, it is also customary for companies to refuse to issue a policy to any person more than 50, or 55, or 60 years of age, for the risk that the events insured against will occur is so great that the rates would equal or exceed the contract benefits.

Property and Life Insurance Contrasted. A totally new element enters into the writing of life insurance contracts. The event insured against, death, is certain. The only uncertainty is when it will come. Mortality

tables show that it is not so likely to come in early years as in the later ones, just as health records show that ill health is more likely in later years. A year-to-year term policy would therefore be much cheaper in the early years but with the certainty of approaching death in later years the annual charge would necessarily be an increasing portion of the indemnity.

Types of Life Insurance Contracts

Assessment Policies. Assessment insurance policies, such as those more commonly written by fraternal orders in the early days of insurance (which brought disrepute on them and on insurance), are one-year-term life contracts. In a group of 1,000 men aged 21, each insured for $1,000, the mortality would be low and fairly even during their youthful years. During the first 23 years, for example, the annual mortality would increase only from 8 to 11. Hence at the end of the first year there would be claims for $8000 to be paid by assessing the remaining 992 men $8.07 each. This is very inexpensive protection. But notice what happens. As the men grow older the annual mortality rate goes up to 14 at age 50, to 18 at age 55, and to 27 at age 60. Unless new men are enticed to join the group, the number left to pay the assessments grows smaller and smaller until finally the cost becomes too great and they drop their insurance.

Term Insurance. This is not to say, however, that term life insurance does not have valuable and legitimate uses. If one wishes maximum protection against a particular hazard for a specified period, term insurance offers the solution to his problem. Suppose a businessman, heavily in debt, desires to protect his family against the hazard of his death before his business is well established, just as he wishes to protect them against the hazard of fire loss on their house. A one-, two-, three-, five-, or ten-year term life policy will give them maximum protection at lowest cost. Or he may secure maximum protection for his children by purchasing a 20-year decreasing-term policy guaranteeing them a stated income during the remainder of that period in case of his death. The annual premium quoted by a certain standard company on a 10-year term contract for $1,000 at age 30 is $8.96 as compared with $19.10 on a whole-life policy which does not participate in "dividends," the least expensive alternative. A contract participating in "dividends," the kind most commonly sold in the United States, would cost $24.20 a year. At the same age a 20-year decreasing-term policy to provide $10 monthly income for the remainder of the 20-year period after the death of the insured would cost $5.95 additional a year, for each $1,000 carried.

Or let us revert to the illustration of the 1,000 young men who are going to take out $1,000 policies for their parents when they graduate next June, at age 21. Being just out of college, their jobs, such as they are, will pay small salaries. Within 5 years they hope to be earning more, but at first they must measure carefully the usefulness of each expenditure. A 5-year term policy will provide the desired protection at an annual cost of $8.28, while the least expensive whole-life policy would cost $14.97 yearly and the premium on a participating policy would be $19.35. At age 26 the nonparticipating whole-life premium would be $2.04 more than at age 21, or $17.01. During that temporary period for the same expenditure the young men could carry $1,800 worth of term insurance protection or have $6.69 a year to spend on something else equally necessary. Compared with a participating policy, the premium of $19.35 on the latter would purchase $2,300 worth of term insurance instead of $1,000 worth, or leave $11.07 to spend otherwise. At the end of that time when earning power had increased the term policy could be converted into another type of contract. Some companies write a "modified" life policy which makes this conversion automatically.

It is quite possible, and in some cases desirable, to use term insurance for permanent protection. The ordinary life policy and variations of it include an element of forced saving which proves expensive in case of premature death. At age 21 it is possible to purchase a term policy expiring at age 65 for $11.79 per $1000. The next cheapest type of policy, a nonparticipating ordinary life, is quoted at $14.97. The next cheapest policy is the participating ordinary life contract which costs $19.35. In the latter two contracts there is a saving feature which provides cash or loan values as the years continue. If, however, a provident individual wishes to separate his insurance from his saving he may purchase term insurance to provide protection for his dependents until age 65. The difference of $3.18 or $7.56 per $1000 can be invested in an annuity contract with the same company. Such an individual would then be paying out either $14.97 or 19.35, *but with this important difference:* in case the insured should die at any time before age 65 under the ordinary life contract the beneficiary would receive the face of the policy and no more; whereas under the plan of separating protection from savings the beneficiary would receive the face of the policy *plus* the accumulated savings during the intervening years compounded annually. For illustration, suppose the insured should die at age 61; under the ordinary life contract the beneficiary would receive $1000 whereas under the other plan the beneficiary would receive $1000 plus the accumulated savings, which, ignoring interest, would amount to $127.20. Obviously this makes

a very great difference on insurance policies amounting to $20,000 or $30,000. If the insured outlived the period of term protection then of course there is no cash value on the insurance contract, but there is a cash value on the annuity contract, which will then begin to pay an annuity income upon retirement.

Level Annual Premium Policies: Whole-Life Insurance. To overcome the objection to increasing term rates with advancing age the level annual premium was evolved. The application of this feature to life insurance is found in the contract described as whole-life or ordinary life. In the lower-age groups when mortality is low the company charges an annual premium in excess of the amount needed to meet the claims then arising. This excess, at age 21, is the difference between the term rate of $8.28 and the whole-life rate of $14.97; namely, $6.69. This surplus constitutes a reserve to meet claims in later years when the annual cost of protection exceeds $14.97. It is invested by the company to yield the highest possible interest consistent with proper regard for security of the principal. On the basis of the American Experience Mortality Table and an assumed rate of interest, usually 3 per cent, the actuaries of the company can calculate with a high degree of accuracy the uniform annual premium which, invested and improved at 3 per cent, will yield the reserve needed to pay claims in later years. It is just as if one were to pay a doctor more than the actual annual cost of medical care during the years between ages 21 and 45 with assurance from the doctor that the annual charge would not increase from age 45 to death, although the actual cost is almost certain to increase.

It is extremely important to notice that this type of contract injects a new feature into life insurance. No longer is the policyholder buying only pure protection at actual cost, except in the long run; he is now saving involuntarily. It is these annual savings which give rise to the later possibility of policy loans and cash surrender value which will be described in the next chapter.

Policies Limiting Number of Premium Payments. While the ordinary life policy provides maximum permanent protection at low cost it has one feature which makes it objectionable to many buyers. That is the necessity of paying annual premiums as long as the insured lives or as long as the contract is continued. As a matter of fact, this objection is more apparent than real, and emanates largely from failure to understand the basic principle that in buying insurance one is buying protection, not making an investment. The admixture of the savings feature with the protective feature in life insurance is logical if understood; but it has given rise to constant confusion in the mind of the average buyer, leading him to believe that unless he or his beneficiaries get back more

than has been paid in, or at least as much, a loss has been suffered. Of course there has been no loss. Rather the buyer has ignored or forgotten or never did understand that the intangible protection for which he paid his premiums has been delivered daily throughout the years. If the insured is obsessed with the belief that premiums paid are lost unless his beneficiaries get back as much as has been paid in or more he can, if he wishes, gamble on the length of his life. If he has reason to believe that he will die at an early age, and does so, then his beneficiaries would get more than the amount of the premiums he has paid, even on a whole-life policy. But if he has any sound basis for such a belief the insurance company also will learn of it from its medical examination and other required information, and will charge him proportionately more, or refuse to insure him. For, let it be remembered, first, last, and always, the insured pays for exactly what he gets in so far as actuaries can determine the cost. Moreover, if the insured were to gamble on that basis he would be much wiser to take out term insurance calculated to terminate not long after his death. But as in the other case the company's medical examiner would discover the likelihood of premature death and if a contract were written at all it would be at rates high enough to yield the face value of the policy at death.

It is certainly not always, nor usually, wise to permit an ordinary life policy to run to maturity. When the insured attains age 65 his children are grown and are no longer dependent. His need then is not protection against premature death but protection against living longer than the Biblical allotment to mortals. The wise procedure then is to drop the ordinary life policy, take the cash surrender value, and buy an annuity contract which will assure him and his wife a definite income as long as they live.

Insurance actuaries have evolved a policy designed to meet the objection on the part of buyers to what they regard as the necessity of paying premiums as long as they live. This is described as the limited payment policy, meaning that the insured pays a stated number of premiums, whereupon the policy is fully paid for. No matter how long the insured lives he need not pay any additional premiums, but the policy is not payable until his death. It should require but small insight to see that the company is merely charging more for each of the limited payments so that the excess reserve, improved at 3 per cent interest, will be sufficient to pay the face value of the contract when payments cease. This is made evident by comparing the 20-payment life premium at age 21, which is $24.55 for a policy not participating in dividends, with the whole-life premium on a nonparticipating policy for the same age, which is $14.97. Under both these contracts the insured is getting

exactly the same thing, protection for his dependents in case of premature death, but under the limited-payment contract he is paying his bill more rapidly. The only difference lies in the fact that in the latter case he knows he must make only 20 payments, while he *thinks* he must pay for the whole-life policy as long as he lives. Actually, this is rarely true. A nonparticipating policy for $1,000 taken out at age 30 costs $19.10 a year. At age 65 the policy reserve will amount to $545, which may be taken in cash, or which may be used to purchase $756 worth of paid-up insurance. Hence the insured might have full protection for his family for 35 years and then stop paying premiums, taking his accumulation in cash or in paid-up insurance. Or if he holds a participating policy and permits the "dividends" to accumulate, a whole-life contract taken out at age 25 will have accumulated a reserve at age 57 sufficient to pay the face value of the contract, according to the actual experience of one company. In other words, a whole-life contract becomes a paid-up policy in 32 years and with much less burden to the insured.

For the manual worker whose years of maximum earning power begin to decline at age 45 or 50 the limited-payment policy has the advantage that he can pay for his protection when he is best able. But for clerical and professional workers whose early salaries are small and whose maximum earning power is more likely to be attained in the years from age 45 to 65 the limited-payment type of policy imposes a wholly unnecessary burden during the years of meager income, with no compensating advantage.

Endowment Insurance. Failure to understand that in buying life insurance one is buying protection for dependents in event of premature death gives rise to another common fallacy, usually expressed in the phrase that "you must die to win." No other expression could reveal better the confusion in the mind of the buyer who holds to that belief. What is it for which "you must die to win"? Obviously the amounts paid in as premiums. That the company has earned those premiums by providing exactly what it sold is beside the point to one who does not understand. So again the actuaries have devised still another type of contract to placate the uninformed but stubborn buyer. This is described as an endowment policy and, if for $1,000, guarantees not only the $1,000 to your dependents if you die prematurely but also $1,000 to you if you live beyond the term of the contract. So the buyer now has what he wants: a policy for which he pays only a stated number of years and which yields its face value whether he lives or dies. What could be better?

But let us inquire into its cost, remembering that insurance is not magic but that the buyer pays for whatever he gets. A company's obliga-

tion under a $1,000 endowment contract is twofold: if the insured dies before termination of the policy his beneficiaries have a claim for $1,000; if the insured lives to the termination of the contract he possesses a demand claim for $1,000. The first obligation is covered by a term policy, for $1,000 the first year, and the second obligation is met by compelling the insured to save an amount each year which, invested and improved at 3 per cent interest, will yield a sum of $1,000 when the contract terminates. The shorter the term the larger the annual saving required. The second year the company need not include a term policy for $1,000, for if the insured should die his savings would be used in meeting the claim. So a one-year term is included which, supplemented by the insured's savings, will meet the policy demands if the policy is terminated. For example, the one-year-term rate is $8.10, while the level annual premium for a 20-year endowment at age 21 is $44.70. The difference of $36.60 represents the first year's saving. In the second year, ignoring interest, the company would include a one-year term for $963.40; in the third year for $926.80; in the fourth year for $890.20, and so continue to decrease the protection coverage until it approaches zero in the last year.

It should be clear now that under the endowment contract if the insured dies his beneficiaries get back his forced savings, with interest at 3 per cent, plus the necessary additional sum from a term contract to total $1,000. This is a so-called insurance policy in which the protective feature is minimized and the saving feature maximized, with greater expense to the buyer. The insured could just as well buy a 20-year-term policy and himself invest the $36.60 each year in an annuity contract with the same company which would yield him 3 per cent annually with equal security and practically the same sum in the twentieth year. In case the insured should die during the twenty-year period the beneficiary of the endowment contract would receive $1,000, while in the alternative case the beneficiary would receive $1,000 from the term policy *and* the accumulated savings plus interest. For illustration, if it were assumed that the insured died in the nineteenth year after paying his nineteenth premium, the beneficiary would receive $1000, the face of the policy, *plus* the accumulated savings which, ignoring interest, would amount to $695.40 ($36.60 × 19).

Why do so many people buy these expensive policies? There are several answers, but the most satisfactory one is that they do not understand the principles of insurance sufficiently to realize what they are buying. That being the case, they are enticed by the alluring prospect of getting their premiums back if they live. In short, they are believers in the fallacy that under term or whole-life insurance "you must die to

win." If buyers generally understood what has just been explained, which is available in any text on insurance, there would be fewer endowment contracts written.

One stock argument for this type of policy is that it provides an incentive to save. If it does it is an expensive incentive; and it is questionable how valid this contention is with modern liberality in cash and surrender terms. Certainly in times of severe depression the number of consumers of insurance who let their high-priced policies lapse and lose all protection is legion. For the typical buyer in lower- and middle-income groups the expensive endowment policy should be shunned.

Other Types of Policies. Insurance actuaries have produced many other types of contracts, such as the family income policy and the educational policy. But it should now be evident that term or whole-life contracts, to which has been added a savings feature, a limited-payment feature, or a settlement feature, are the basis for all these variations. If this fact is kept in mind as one buys insurance and one deals with a representative who is informed and reliable, it is unnecessary to attempt to explain these newer developments. In fact, it would be futile in view of the speed with which they are devised. One of the five largest mutual insurance companies in the United States writes 136 different policies. An insurance company will write a contract containing almost any special features desired, just as a builder will construct a home to suit individual peculiarities, *if the buyer is able and willing to pay the price.*

Group Insurance. Group insurance has spread so phenomenally in recent years, however, and holds such great possibilities for the future, that every consumer of insurance should know what it is and whether to buy it if the opportunity arises. As the term suggests, this type of insurance is written on a group of lives, rather than on individual lives. If the group is large enough the company is safe in forgoing medical examination, thereby reducing costs. Administrative expenses are further reduced by issuing a blanket contract, in place of individual policies, and by making payment in one check, thereby eliminating hundreds or thousands of bookkeeping entries. The protection cost is reduced to a minimum by use of the yearly renewable term contract. While the rate per $1,000 varies according to the group, the employer pays the variable amount and the employee pays a fixed premium of $7.20 a year, regardless of age (if within the age limits) and without medical examination. If one leaves the employ of a company providing group insurance it is usually possible, without passing a physical examination, to convert the amount of individual coverage to another type of contract by paying the premiums scheduled at age of conversion.

In 1942 over $8,000,000,000 worth of group life insurance was sold

in the United States. For the first time in the history of life insurance the annual volume of group life insurance exceeded that of ordinary life. The total of group life insurance in force at the beginning of 1943 was $20,000,000,000. The amount of group life insurance which is available to an individual is usually related to one's annual income. It is assumed that in case of premature death the proceeds of a group life insurance policy will yield the same amount that the insured would have provided to his family if he had lived. Such a sum will enable the beneficiaries better to make the adjustment in their mode of living. For those whose life insurance programs are not completed it may be said without qualification that group life insurance provides a good opportunity to secure protection at low cost.

Annuities. In times of depression when investments fail and banks close, persons who thought they had provided an income for their old age find themselves in distress. Another, and larger, group who were improvident in early years, or whose income was too small to permit saving for the future, also find themselves dependent in old age. For all these groups the surest security against this hazard is an annuity contract. An annuity contract is a form of insurance which guarantees a fixed income to the annuitant during the later years of life. The two most common types, the ordinary life or immediate annuity and the deferred annuity, may be explained by an illustration.

Reverting to the parents of the 1,000 young men who will graduate next June, let us assume they have all reached age 65. Their children are now graduated from college and are independent. Death is nearer and, because so certain, there is no need for providing a cash income in the event of an early demise. It is far more important to assure themselves an income which will not fail even in a depression, so they will not be a burden on their sons who are struggling to set up their own homes and protection programs.

The wise procedure is to convert all assets into cash, using the proceeds to buy an immediate annuity. At age 65 the normal expectancy of life is 12 years 9 months. If the cash surrender value of all but $1,000 worth of life insurance is $10,000 and the cash yielded by other assets is $5000, the prospective annuitant can buy a guaranteed cash income of $98 a month for life if he purchases an ordinary annuity contract. Not only does the annuitant receive as safe an investment as can be bought, but he also gets more than twice the return he could normally expect. If he invested his $15,000 with proper regard for security he would do well to secure an average rate of 4 per cent, which would yield $600 annually. By purchasing the annuity he gets $1176 a year, almost doubling his annual yield. There is no magic in this procedure. It is

made possible because he is now using principal as well as interest, and the company can afford to guarantee $98 a month because its actuaries have calculated that the principal and interest will yield that amount for 12 years and 9 months, at their assumed rate of interest.

If one of the annuitants dies after 9 years the unpaid portion of his principal goes to pay some other annuitant who lives 15 years and 9 months. Objection to this last feature is met by another form of contract which guarantees to return to the annuitant's beneficiaries or estate the unpaid portions; but of course the monthly annuity would be smaller under such a contract. Another variation, and a useful one, is that known as a joint and survivorship annuity, which guarantees the income to both parents as long as either one lives. Again, the $15,000 would buy a smaller monthly income under this plan. On the other hand, if the purchase of a life annuity is postponed to age 70, $15,000 will buy a guaranteed life income of $116.25 monthly.

To illustrate the deferred annuity let us turn again to the young graduates. During their first 10 or 15 years out of college their limited incomes will be absorbed in living expenses and in buying protection for their families. But when they reach age 35 or 40 their incomes will be larger, their insurance estate completed, and their next concern will be protection against old-age dependency. By purchasing a deferred annuity contract at age 35 which requires an annual premium of $120 the buyer may expect an annual income of $415 beginning at age 65. If the annuity be deferred to age 70 this premium will purchase an annual income of $616, since the expectancy of life is 5 years less. This, supplemented by the ordinary annuity which the cash value of his insurance and other assets will yield at that time, will assure a monthly income during old age that will make a parent financially independent when his children are setting up their homes.

At the beginning of 1939 the 26 largest legal reserve life insurance companies had 868,000 individual annuity contracts calling for annual payments to annuitants of $432,000,000. In addition there were 600,000 group annuity contracts calling for annual payments of $103,000,000.[1]

Beginning in 1935 some forty to fifty million people became involuntary participants in a national program providing for retirement annuities. In 1939 the Social Security Act was amended. The formula for calculating retirement incomes was amended and insurance protection was provided for widows, orphans, or parents of insured workers. Under this national program retirement income payments began in January,

[1] Temporary National Economic Committee, *Study of Legal Reserve Life Insurance Companies*, Monograph No. 28, p. 329, United States Government Printing Office, Washington, 1941. Hereafter referred to as TNEC, *Monograph 28*.

1940. For young men adequately to plan their insurance and retirement programs in the future, it will be essential to dovetail one's personal insurance plan with the Social Security program. The average buyer of insurance will need expert assistance in working out the most effective combination of plans. A helpful source of information is given in the footnote below. It is almost certain, however, that most buyers will need and wish to have the help of an insurance counselor.[1]

Summary

This chapter has emphasized the hazards to life, limb, health, and wealth which hover over every consumer. Insofar as possible we should prevent these losses from befalling, by exercising precaution in our living habits. No precaution can prevent death, however, and illness or accidents happen in spite of our greatest care. Insurance is the modern means of spreading the risk of loss arising from these causes. Insurance does not prevent the occurrence of the event insured against, but it does reimburse the insured in whole or in part for the financial loss incurred. There are as many different kinds of insurance policies as there are hazards hovering over us. The problem for the wise consumer is to know which contracts to buy. No general answer can be given, because individual needs are so variable. Let it be emphasized once more, however, that in buying insurance one is buying protection. If maximum protection at minimum cost is desired it may be secured by purchasing term insurance to meet temporary hazards. If maximum permanent protection for dependents against premature death of the insured is desired at minimum cost it may be secured by purchasing a whole-life policy. Only in exceptional cases should limited-payment or endowment contracts be considered. For health and accident coverage one should compare the contracts offered by several reputable companies as to cost, benefits, and loopholes. To secure protection against old-age dependency, in most cases, one should start buying a deferred annuity contract as soon after age 35 as possible, unless the prospective retirement income under the Social Security Act is adequate. Upon reaching retirement age the best plan, in most cases, is to convert all assets into cash, except $1,000 worth of insurance to cover burial and last illness expenses, and to buy an ordinary annuity to supplement the deferred annuity.

Those who are financially able to carry out such a program will have taken every possible precaution to provide for themselves and dependents protection against the many hazards of an uncertain world.

[1] For information on how to combine your Social Security and personal insurance program see Francis, Bion H., *What Will Social Security Mean To You?*, American Institute for Economic Research, 54 Dunster Street, Cambridge, Mass., $1.

QUESTIONS FOR DISCUSSION

1. Do you have any life insurance? If so, why?
2. How much life insurance does your father carry? How much should he have?
3. Why would it not be a good idea to organize a mutual insurance company on your campus to insure the lives, health, and automobiles of all students?
4. Does your father carry any term insurance? How much did you know about this type of contract before reading this chapter?
5. Why do companies write limited-payment policies? Would you purchase this type?
6. How can an annuity double the annual yield of your investment?
7. Why is group insurance usually cheaper for the individual participant? Is it sound?

PROBLEMS AND PROJECTS

1. List all the hazards hanging over you; what kinds and what amounts of insurance should you carry?

2. What risks are incurred by your father? What kinds and what amounts of insurance should he buy?

3. Compare rates on automobile insurance of all kinds in your vicinity with those in another area; if you live in a city compare suburban and country rates, and if you live in one of the latter regions compare city rates. How do you account for the differences?

4. Apply the procedure in problem 3 to fire insurance rates.

5. If you live in an industrial area find out how many employees are covered by group insurance and for what amounts. Compare individual with group insurance rates.

6. Ask at least three insurance agents to draw up for you a recommended program of life insurance. Compare these programs with one another and with your own ideas; do you think the programs were all well designed to meet your risks at lowest cost?

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Buying Protection: Insurance Practices

Insurance As a Business

Organization for Underwriting: Mutual Companies. Since the function of insurance is to spread the risk over a large number, substituting for a large, uncertain loss a smaller, certain loss, it is quite natural that groups of individuals sharing the same interests and risks should organize themselves into a risk-bearing association. Broadly speaking, this is the way a mutual association or company is organized. All the farmers in a township or county or state may band together for fire protection. Or we might think of the 1,000 parents of next June's graduates as forming a mutual organization to protect themselves against possible fire loss to their homes. In organizing, a membership fee may be charged to create a capital reserve for contingencies. Fire losses during the year may be paid out of this reserve, but it will be replenished by assessing each member of the group an amount sufficient to cover the losses sustained. There is no reason why such a mutual may not operate on the reserve basis, levying its charge in advance so the insured will know just about what his fire protection is going to cost. Many mutuals do operate on this basis, usually retaining, however, the right to assess members a limited amount to make up any unusual losses. The distinctive feature of the mutual is the retention, in theory if not in practice, of control by the policyholders. It is their mutual undertaking whose responsibilities and benefits are mutually shared. For the smaller, local mutuals this retention of control is most likely to be realized. And in the field of property insurance this method of financing is also usually satisfactory since, as we have seen, there is no certain destruction of the wealth insured. Administratively, the costs are likely to be lower, though there may be less efficient management. An added advantage is that members of a mutual are engaged in a co-operative enterprise and as such are not likely to cheat themselves or their associates. This practically eliminates the arson hazard which looms so large in the problems of large stock companies. That this method of organizing to protect owners of wealth against loss is fundamentally sound is attested by the 2,400 such associa-

tions operating in the United States with contracts covering billions of dollars' worth of wealth.[1]

It is important to check this type of organization, however, against that one of four basic principles of sound insurance which prescribes that the number of objects or lives insured must be numerous enough for the law of large numbers to apply. By its very nature a local mutual runs counter to this principle, but if the objects are widely scattered geographically this disadvantage is partly offset. A second serious problem is that of management. As long as the mutual is small the management is likely to be more honest and well-meaning than efficient, and when the association grows larger, management is more likely to be efficient but there arises the question, efficient for whom? And as the number of policyholders increases, the likelihood that each one will take an active interest in the management grows less, while the likelihood that the hired managers will assert more and more control grows greater.

In the realm of life, health, and accident insurance the logical development of mutuals for protection proceeded through fraternal orders, labor unions, and groups of men with common hazards and interests such as traveling salesmen, ministers, and teachers. The early success of mutuals for protecting wealth naturally led to the belief that the same principles could be applied in assuring protection against illness, accident, and death. Since illness and accident, like fire, are not certain, the same assessment method can be used safely and satisfactorily if proper regard is given to selection and diversification of risks assumed. But since death is certain and more likely to occur in later years a contract guaranteeing $1,000 indemnity at death can be fulfilled at reasonable cost only if a reserve is accumulated to meet that certain claim. It was shown in the preceding chapter that while annual assessments are low during early years of the policy they necessarily increase in the later years, unless a number of young men can be induced to replace the ones who have died. But experience has shown that young men are loath to join a group whose costs are mounting and some already in drop out as assessments grow larger each year. The ultimate outcome is certain, and many such insurance organizations have failed, bringing loss and disappointment to members and disrepute on the group and on insurance. Insurance as an economic institution has not yet completely lived down the reputation gained as a result of fraternal assessment failures.

There is no reason, of course, why a mutual cannot apply the reserve principle successfully, as has been done since the distinguishing charac-

[1] Huebner, S. S., *Property Insurance*, p. 65, D. Appleton-Century Company, New York, 1938. For a more detailed description of types of underwriters read Huebner's entire chapter 5.

teristic of life insurance has been more widely understood. Also there has been an increasing tendency on the part of state governments to compel adoption of the reserve principle. If a fraternal mutual charges a level annual premium, thereby building up a reserve, under rigid state regulation, it can provide perfectly safe protection to its member policyholders, provided the risks are large enough in number, diversified as to occupation, and scattered geographically. Failure to write contracts in accord with the last three qualifications may result in unusual claims arising out of a localized epidemic or other similar catastrophe. Administratively, such mutuals have a real advantage in that they are operated co-operatively to render protection at cost rather than to yield a profit to a small group of owners.

Practically every defect of the small local mutual is overcome by the large national and international mutual. Some of our largest life underwriters who number their policyholders by hundreds of thousands are organized as mutuals. The number of policyholders is large enough for proper application of the law of probability; their occupations are widely diversified and their residences so widely spread geographically that only a national calamity could embarrass the reserves. Theoretically these huge organizations are owned and controlled by policyholders, but only theoretically. The very number of policyholders and their geographic diffusion, so advantageous actuarily, are fatal to effective control. The result is control by a few, who have shown in some instances that there are other ways of dipping into surpluses than by declaring dividends. The most simple is by voting themselves large salaries, to be supplemented by bonuses and such emoluments of office as expense accounts, travel at home and abroad, long vacations with pay and expenses, free lunches, free health and accident policies, and free service in company-owned sanatoria.[1] In 1938 the presidents of the Metropolitan Life Insurance Company and the Mutual Life Insurance Company each received salaries of $125,000; the presidents of the Prudential Insurance Company of America and of the New York Life Insurance Company were paid $100,000; while the president of the Equitable Life Assurance Society was paid $75,000. In addition to these presidential salaries, numerous vice presidents received payments ranging from a minimum of $10,000 up to $75,000. In the six largest mutual companies 2,465 executives received $5,000 or more in salaries, compensation or emoluments, not including commissions. Metropolitan alone paid $5,000 or more to 1,052 executives, 23 of whom received

[1] Schnitman, L. Seth, *How Safe Is Life Insurance?*, The Vanguard Press, New York, 1933, gives a detailed exposition of this side of mutual management, especially in chaps. 3 and 4.

$25,000 or more. By contrast salaries and other emoluments paid to the principal executives of stock life insurance companies were found to be less. The highest recorded salary for the president of a stock company was $65,000, the average being $34,364 compared with an average of $53,664 for mutual officers. In many cases, however, the financial benefits accruing to stock company officials are not limited to their salaries since they frequently hold considerable blocks of stock.[1]

As a result of this situation, instead of mutual company quoted rates being lower than those of stock companies they are usually higher. They should be lower, as some net rates are, because mutuals have no profits to earn for stockholders and competition should have reduced rates to their lower level of cost. Actually it has worked the other way. Mutual rates have been pushed up on a par with stock company rates and the surplus spread, not in "profits" but in emoluments of office and in dividends. Mutual company officials point with pride to their low net cost over a 10- or 20-year period but when a policyholder has to pay $19.35 per $1,000 for insurance instead of $14.97 he is compelled to carry less protection. Lower gross rates are to be preferred over large "dividends." Mutual company gross rates could be much lower than they are, as has been shown by the Massachusetts Plan, and will be reduced when the ones in whom authority really rests assert their power. When a mutual company agent approaches you ask him to what extent policyholders really control his company; what provision is made for them to vote, and to what extent they have a voice in determining home office salaries, agents' commissions, other selling costs and expenses, and to what extent they help to decide how large the "dividends" will be. In all probability the agent will not know. If he does not, insist that he get satisfactory answers from the home office. When you and several thousand other policyholders and prospective buyers become persistently and annoyingly vocal you may succeed in recapturing for mutual policyholders some measure of control, with resulting lower rates. In this connection it is significant to observe that the 1938 salaries of four of the five company presidents listed above were considerably lower than they had been in 1932. In the year 1932 the Metropolitan president drew $200,000, the New York Life and Prudential presidents $125,000 each, while the president of the Equitable received $100,000.[2]

Stock Companies. Stock companies, as the name suggests, are profit-seeking corporations which issue capital stock, the owners of which expect to receive dividends, as on any other corporate stock. They alone control the company, the policyholders being in the same relative posi-

[1] TNEC, *Monograph 28*, *op. cit.*, pp. 96, 97.
[2] *The Nation*, April 26, 1933, p. 459.

tion as the purchaser of a commodity or service sold by any other commercial company. A flat premium is charged, which is low and definite in amount and time of payment, and which eliminates all uncertainty. When the policyholder buys a contract he knows what he is getting and exactly what it will cost. He need not speculate with the company on anticipated earnings, mortality, and management cost, as in the case of mutuals; the corporation does all the speculating, paying to its shareholders, rather than to the policyholders, any surplus accruing. Thus the premium on an ordinary life contract at age 21 quoted by a stock company is $14.97 per $1,000 as compared with a mutual premium of $19.35. The difference represents a "loading" charge, part or all of which *may* be returned to mutual policyholders if claims and management costs are substantially less than income from premiums and interest. It is impossible to compare satisfactorily the net cost of protection under the two plans except historically, for the future "dividends" of mutuals are uncertain. Any such comparison becomes one of companies rather than of types of companies. Clearly, the initial cost of protection is lower for the stock company, and for the man with limited income who wants maximum permanent protection at lowest cost the stock company policy is the cheaper.

With respect to management and control there is little real difference between the two types of companies. The economic doctrine of self-interest applied to stock insurance companies leads to the conclusion that owners will hire the most efficient managers to insure larger profits for themselves. Actually, if the number of shareholders is large the control of the company will fall into the hands of a few, probably the ones who own the largest blocks of stock, through failure of large numbers of small holders to participate in elections. This is exactly what happens in large mutual companies. In 1937 only 2.5 per cent of the possible votes were actually cast in the election of officers for the Prudential Life Insurance Company. Yet that was the largest vote of any of the twelve leading companies. The Metropolitan Life Insurance Company and the Provident Insurance Company were the only other two for which the percentage of possible votes actually cast was greater than 1 per cent; all the others were less than .8 per cent. According to evidence presented to the Temporary National Economic Committee, the reason Metropolitan and Prudential had a relatively high vote was because they were the only two of the twelve companies that used their agency force in soliciting votes. Agents were assigned batches of ballots which they were supposed to have policy holders sign. In order to save time for themselves, the agents commonly signed ballots for each other.[1] As of

[1] TNEC, *Hearings*, Part 4, pp. 1313–1322 and p. 1401.

December 31, 1942, Metropolitan estimated that its 30,000,000 policyholders held 40,000,000 policies. In the 1941 elections for the board of directors, there were 167 votes cast in person. No votes were cast by proxy, but there were approximately 189,000 votes cast for each director by mail. The New York Life Insurance Company with 2,200,000 policyholders reports 68 votes cast in person at the 1943 election of directors, with 2 cast by mail and none by proxy. "On the basis of the evidence adduced, it cannot be said that the policy holders had any control over the management of the mutual companies. The putative rights of the policyholders to select and elect directors are of no practical value. The directors are completely self-perpetuating."[1]

The controversy over the relative merits of the two types of companies cannot be resolved in this short discussion. It is important that the buyer know something about both. In the United States large mutuals dominate the field of life insurance. Although there are only 74 mutual companies compared with 216 stock companies and 7 mixed, the mutual companies in 1939 had assets of more than $22,000,000,000 compared with $5,000,000,000 for stock companies and $219,000,000 for mixed companies. Moreover, the mutual companies had $82,000,000,000 worth of life insurance in force compared with $28,000,000,000 for stock companies and $740,000,000 for mixed companies. On paper the mutuals appear to have all the advantages, but in practice the gains are partially lost because policyholders are either unable or unwilling to assume responsibilities of ownership when the group grows unwieldy. Keeping all these things in mind, remember, too, that premiums do vary among companies, contrary to a common belief that all rates are the same or nearly so. Among 23 of the largest and leading life insurance companies writing participating policies, the annual premium on a $1000 full life policy issued at age 35 ranged from a minimum of $24.58 to a maximum of $28.11. The net cost at the end of the twentieth year ranged from a minimum of $36.20 to a maximum of $133.94. The standard annual premium for nonparticipating policies sold by stock companies was $21.42 at age 35. The 20 year net cost for a group of 7 stock companies ranged from a minimum of $117 to a maximum of $132.[2]

Whether one buys from a stock company or from a mutual, the premiums of several companies should be compared and, if all other factors appear to be equal, the deciding element may prove to be the cost. Yet the investigations of the Temporary National Economic Committee disclosed the hitherto unknown fact that "the principal life insurance companies have for several years undertaken to eliminate rate competition by means of inter-company agreements and 'gentlemen's' under-

[1] TNEC, *Monograph 28*, p. 14. NEC, *Monograph 28*, p. 242.

standings. Efforts in this direction have been highly successful and, as might be expected, the agreements have been extended to bring about uniformity in certain underwriting practices and in certain policy provisions as well." The leading Eastern companies, particularly the stock companies, have entered into agreements to fix the rates for ordinary life insurance; this is true of both participating and nonparticipating types. In addition to uniformity in rates, these intercompany agreements also established a uniform basis for surrender values, uniform settlement options, and regulations concerning the exchange of medical information and the control of agency commissions and practices.[1]

Mixed Companies. A combination of the distinctive features of mutuals and stock companies results in the so-called mixed company. Organized as a stock company and owned by the stockholders, this type of company usually offers two types of policies, the nonparticipating and the participating. The former is a straight stock company contract, but the latter embraces the mutual principle of sharing excess earnings with the policyholders. Since there are two groups to share the earnings there are many different plans designed to benefit one or the other, one of the most common being the provision that stockholders are limited to 10 per cent of the surplus, the remaining 90 per cent being reserved for distribution among policyholders. Control of this type of company is certain to rest with the stockholders, through some restriction such as granting the right to vote only to holders of policies with a face value of $5,000 and restricting the number of directors which policyholders may elect. Theoretically, this hybrid type of company possesses no real advantage, but in practice it does offer possible gain. This is because the mutual is not as low in cost as it should be, while the straight stock company has no way of sharing excess earnings with policyholders. The mixed company participating policy may therefore prove to be the lowest cost in the long run and even lower in the short run than the rate of large mutuals. The Sun Life Assurance Company of Canada is one of the larger companies of this type doing business in the United States.

Protecting Buyers

Need for Regulation. Regardless of the type of organization adopted for engaging in the business of selling protection, it is clear that the officials of insurance companies hold a fiduciary position which carries with it grave responsibilities. While the exact number of insurance policyholders in the United States is unknown, there are about 43,000,000 ordinary contracts and 90,000,000 industrial policies, besides 30,000 group contracts. It is estimated that these 133,000,000 contracts are

[1] TNEC, *Monograph 28,* pp. 141–152.

owned by 50,000,000 to 70,000,000 individuals, who had in force $139,000,000,000 worth of life insurance as of January 1, 1944. Most of these contracts require premium payments in excess of actual current protection cost, resulting in huge reserves which must be invested to yield at least the guaranteed rate of interest, usually 3 per cent, with proper regard for safety of the principal. An estimate as of December 31, 1942, placed the amount of insurance company assets at $33,000,000,000. As of January 1, 1944, the Institute of Life Insurance estimated that insurance company assets totaled nearly $38,000,000,000.[1] Three dangers for policyholders arise. One is the temptation of officers to use some of these vast sums for personal benefit. This is covered by the general term embezzlement and is guarded against by statutes, of varying effectiveness, declaring such acts criminal in nature and punishable as such.[2] A second danger, and a more serious one in practice, is that powerful officials in control of the company may, by legal but unethical means, secure for themselves a portion of these huge reserves. In the case of mutuals the theoretical power of policyholders to elect officials and, in the cases of stock and mixed companies, the theoretical power of stockholders to elect officers, has been the chief safeguard. How ineffective it is in practice has been shown. A third danger to policyholders' reserves is the ever-present possibility of loss resulting from honest but unwise management of investments. If human culpability could be eliminated this risk would persist, but when both dangers are present the policyholder stands to lose. The amazing extent to which these three dangers threatened the savings of millions of persons was first revealed in 1905 by the investigation of the Armstrong Commission in New York, the home state of four of the "Big Five" mutual companies. It was the conduct of that investigation which attracted national attention to the young attorney Charles E. Hughes and started him toward the governorship of the state. Additional revelations of malpractice resulted from the Pujo investigation of 1913.[3]

On April 12, 1938, President F. D. Roosevelt recommended an investigation of the extent of concentration of economic power in the United States. Congress established the Temporary National Economic Committee, which in turn authorized the Securities and Exchange Commission to make a complete study of legal reserve life insurance

[1] *New York Times*, January 1, 1944. [2] See Baarslag, Karl, *Robbery by Mail*, Chapter XIII, Farrar & Rinehart, New York, 1938.

[3] Hendrick, B. J., *The Story of Life Insurance*, McClure, Phillips & Company, New York, 1907. There are several sources to which you may turn for the details of these investigations, including the *Reports* of the two Commissions, and the *Annual Reports* of the Commissioner of Insurance for New York. A journalistic account is given by Sullivan, Mark, in *Our Times*.

companies. A summary of the findings with reference to insurance companies was published as *Monograph No. 28*. Sections 3, 4, 6, and 7 deal with aspects of company management and practices which led to personal gain for officers or directors.

Although the business of insurance companies is national and international in scope the Federal government was powerless to act, since the selling of insurance had been held not to be interstate commerce within the meaning of the constitution.[1] The findings of the Temporary National Economic Committee might well have led to an effort on the part of the Federal government to find a way to exercise regulatory power. But the outbreak of war in 1939 quickly diverted Congressional attention. As a result, policyholders had to look for statutory protection to the state in which the company was chartered and the state in which they bought their contracts. After the Armstrong and Pujo investigations, the state of New York imposed what were then regarded as fairly rigid restrictions on investment of reserves, limiting officials to the purchase of specified securities. But the growing tendency by companies to mix the saving feature with the protection feature has resulted in their growth as demand banking institutions with consequent weakening of their position as pure underwriting companies. The seriousness of this situation was revealed in the decade 1930–1939. During that period 188 life insurance companies discontinued operations. For purposes of comparison it may be stated that in 1939 there were 365 legal reserve life insurance companies in operation. Most of the 188 companies which discontinued were involved in mergers or reinsurance arrangements, as a result of which their cessation of operations did not necessarily involve losses to policyholders. There were 19 failures, however, which indicated an initial loss to the policyholders of $138,000,000. These failures were caused almost entirely by "flagrantly bad investment policies, policies which in many cases were tantamount to fraud and breach of trust on the part of company management." Regardless of the underlying causes of the failures, most of those in the decade referred to were precipitated by the depression. As a result of the widespread use of convention values and moratoria, the number of failures was undoubtedly lower than it would have been otherwise. Convention values

[1] On June 5, 1944, the Supreme Court overruled a 75-year precedent by declaring that insurance companies are engaged in interstate commerce and therefore subject to the Sherman Anti-Trust Act. The decision, affecting fire insurance companies, did not make it clear whether life insurance companies were included, but it was generally believed that all insurance would be held to be covered. The full significance of this decision cannot be ascertained for some time. It was reported that insurance companies would ask Congress to pass a special law declaring that insurance is not commerce. *New York Times*, June 6, 1944, pp. 1, 10.

were arbitrarily assigned by state insurance commissioners enabling the companies to carry their securities in their annual statements "at a valuation in excess of their then market." As of December 31, 1932, convention values exceeded market values of the securities of the 26 largest companies by $1,124,406,000. That was equal to an excess valuation on the balance sheet of 20 per cent. In succeeding years the convention values have been adjusted gradually to current market values.[1] Apparently state regulation of legal reserve company investments has not been altogether successful. Nor has there been any real change in control of the big companies, all the evidence pointing to the conclusion that the so-called mutuals are actually controlled by a small self-perpetuating group of officials, with the same condition prevailing in the case of stock companies.

By and large the legal reserve life insurance companies of the United States are financially strong and sound. The TNEC investigation did disclose, however, certain practices on the part of company officials and agents which call for correction. There is need for a revamping of insurance control laws with a view to benefiting the buyer of protection. Since four of the "Big Five" insurance companies are chartered in New York, that state is logically the one in which such a movement should begin. This is a program to which insurance buyers must give active support if they wish more assurance that their beneficiaries will enjoy the protection which the insured think they are providing.

The Massachusetts Plan. One tangible result of the Armstrong Committee investigation in 1905 was the establishment in Massachusetts in 1907 of a wholly new type of insurance institution. After surviving bitter attacks of vested interests in private insurance companies the state government adopted a plan permitting established mutual savings banks to write life insurance up to a maximum of $1,000 on a life. Although there are now thirty issuing banks individual purchasers are limited to a maximum of $25,000 coverage.

All agents are eliminated under this plan, the policies being sold over the counter at cost. In addition to the 30 underwriting banks there are 173 mutual savings banks, national banks, trust companies, and co-operative banks acting as agencies. By eliminating expensive selling methods and excessive management costs, net premiums per $1,000 of insurance are considerably less than mutual company rates. In 1938 total expenses of savings-bank ordinary insurance represented approximately 8 per cent of premium income compared with 13 per cent for all ordinary insurance and 25 per cent for industrial insurance. In 1939 the ratio of salaries and commissions to premium income was roughly

[1] TNEC, *Monograph 28*, pp. 101–136.

3 per cent for savings-bank ordinary insurance, 12 per cent for company ordinary insurance, and 20 per cent for industrial insurance. In 1938 the ratio of actual to expected mortality losses for savings-bank insurance was 34 compared with 57 for all ordinary insurance (including the savings bank insurance), and 43 for industrial insurance. As a result of these differences a comparison of the net premium for a $1000 policy issued in 1930 at age 35 based on actual dividend history during the following ten years shows an average net payment for ten private companies of $20.66 compared with $16.29 as the average of 15 savings banks in Massachusetts. In answer to the prediction that people will not buy insurance but must be sold by high-pressure methods the mutual savings banks of Massachusetts point to more than 253,000 policies guaranteeing protection to the extent of $230,000,000.[1]

After many years' effort the New York legislature adopted a greatly modified plan of savings-bank life insurance in 1938. Among the several points of difference between the plans of the two states the most serious is the New York limitation restricting buyers to $3,000 worth of insurance, designed to protect mutual and stock companies from full competition with the new system. At the end of May, 1943, there were 36,553 savings-bank policies in force in New York for a total insurance coverage of $31,494,000. The insurance is now offered by 44 mutual savings banks throughout the state. As in Massachusetts, the economies of savings-bank life insurance have been demonstrated in New York. In most cases the gross annual premium is considerably less than that of private insurance companies, and likewise the net cost of insurance protection is almost always less than that of the private companies.

Early in 1941 the legislature of Connecticut enacted a law permitting the establishment of savings-bank life insurance in that state. The system is similar to those of Massachusetts and New York. In the same year proposals to extend savings-banks life insurance were considered by the legislatures of Maine, Maryland, New Jersey, Pennsylvania, and Rhode Island.

Savings-bank life insurance was designed originally to provide a safe, sound, and less expensive substitute for "industrial" and ordinary life insurance. "Industrial" or "weekly premium" insurance has been

[1] For details of this plan see literature issued by the Savings Bank Life Insurance Council, 80 Federal Street, Boston; a study by CASADY, Clyde S., *Massachusetts Savings Bank Life Insurance*, The Lothrop Press, Springfield, Massachusetts; United States Department of Labor, Division of Labor Standards, *Savings-Bank Life Insurance*, Bulletin No. 44, Washington, 1941; MASON, A. T., *The Brandeis Way—A Case Study in the Workings of Democracy*, Princeton University Press, Princeton, New Jersey, 1938; United States Department of Labor, Bureau of Labor Statistics, *Operation of Savings-Bank Life Insurance in Massachusetts and New York*, Bulletin No. 688, United States Government Printing Office, Washington, 1941.

widely sold in the United States since 1876. It is purchased most commonly among low-income families and is acquired chiefly for the purpose of providing payment for funeral expenses. By 1938 there were 138 companies writing "industrial" insurance. There were close to 90,000,000 policies in force, representing some $21,000,000,000 of insurance. The Prudential Insurance Company and the Metropolitan Life Insurance Company together wrote 73 per cent of all "industrial" insurance. A comparison of the annual gross premiums for $1000 of ordinary life insurance at age 35 shows an average rate of $26.27 for ten private companies, $23.90 for fifteen Massachusetts savings banks' policies, and $40.56 for "industrial" policies issued by three large companies.

Unfortunately, the record does not show that savings-bank life insurance in Massachusetts is fulfilling its purpose. Compared with $162,000,000 of savings-bank ordinary insurance in force in 1939, ($230,000,000 in 1943) there was $1,169,000,000 worth of "industrial" insurance in force. These figures are confirmed by the results of a survey of 2,132 Massachusetts families having low incomes. It was found that 92 per cent of all the families interviewed were carrying insurance or had done so. There were over 10,000 policies in force in the 1,666 insured families. As many as 83 out of every 100 persons in insured families were covered for an average of $683 each. The average insured family spent practically 5 per cent of its income for insurance premiums; in some cases the percentage was as high as 24. But the predominant form of policy was "industrial" insurance. That was the type of insurance protection purchased by practically 80 per cent of the insured persons.

Although some of the more extreme evils of "industrial" insurance have been eliminated or modified, it is still true that that type of insurance is too expensive. Moreover, it is sold by high pressure methods to people who do not need it. The survey revealed an overloading of policies, too large a percentage of family incomes spent on insurance, an uneven distribution of coverage among family members, and much too great use of endowment and limited payment policies. As a result of all this there was a very high lapse rate. "Industrial" insurance is written primarily to provide funds for undertakers rather than income for dependents of the insured.

High pressure selling by 100,000 agents accounts for the prevalence of "industrial" insurance throughout the United States. Metropolitan and Prudential together employ 40,000 "industrial" agents. As a result of overselling the wrong kind of insurance to the wrong people, 95 per cent of "industrial" policies terminate before their ultimate purpose is realized. One case of overloading and bad distribution was that of a longshoreman whose income supplied the sole support for his wife and

son. In May, 1938, he had 44 insurance policies, 4 of which were written on the ordinary life plan and 40 on the "industrial" plan, for a total of $18,000 coverage. The annual premium was $926.89, which figured out to a cost of $51 per $1000, and represented 55 per cent of the father's yearly income.[1]

Compare the foregoing statements based on field and statistical surveys with the following lines taken from a paid advertisement of the Metropolitan Life Insurance Company in 1943:

> "In keeping with American individualism, life insurance itself is individualized—tailored to fit the hopes and ambitions, the needs and income of each policy holder. And each family's insurance program, shaped according to its own particular needs, has been made possible by the untiring work of the life insurance agent. It is the agents who teach people to understand and appreciate the benefits of life insurance. Through their efforts in times of peace, agents helped some 65,000,000 Americans to take advantage of the flexible, individualized service characteristic of American life insurance."[2]

At this point the question very naturally arises as to why savings-bank life insurance has not been adopted in a larger number of states. Of course, no certain answer can be given, but bitter opposition on the part of mutual and stock company officials to the original plan and to recent efforts to secure this type of legislation in New York and Connecticut provides a clue as to the reason for the failure of bills to reach the floor of the several legislatures in which they have been introduced. The Temporary National Economic Committee established the fact that the Association of Life Insurance Presidents is a lobbying agency for private insurance companies. It was organized in 1906 and as of 1938 numbered 67 legal reserve life insurance companies which wrote 85 per cent of the life insurance business in the United States. The Association has representatives in every state. In the four years 1935–1938, total disbursements of the Association were approximately $1,700,000, of which some $560,000 were described as "legislative disbursements." Testimony before the Temporary National Economic Committee described in detail how the life insurance lobby prevents

[1] TNEC, *Monograph 28*, pp. 250–304; *Monthly Labor Review*, vol. 51, *Life Insurance Among Low Income Families*, pp. 1335–1351.

[2] *Business Week*, February 6, 1943, p. 23. For a defense of weekly premium industrial insurance and a contention that it does not cost much more than ordinary insurance, as commonly believed by critics, see Howell, Valentine, *Comparative Net Cost Factors in Ordinary, Group and Industrial Insurance*, pp. 132–135, in McCahan, David (Editor), *Life Insurance: Trends and Problems*, Huebner Foundation Lectures, University of Pennsylvania Press, Philadelphia, 1943.

the passage of proposed legislation it does not like. First of all it attempts to persuade the author of a bill to withdraw his proposal; failing that, an effort is made to have the bill killed in committee; failing that, the next step is to have a competing bill introduced; if, in spite of those tactics, the bill passes either house in any one of the state legislatures, it must then go to the other house, where the foregoing tactics are repeated.[1]

As a result of these revelations and of a growing realization of the advantages of savings-bank life insurance, it is possible that this form of insurance protection may be made available to low-income consumers in an increasing number of states. In 1939 a resolution was adopted by the Sixth National Conference on Labor Legislation, urging labor officials, civic groups, employers, and labor organizations to consider the possibilities of legislation making savings-bank life insurance available in the 46 states whose citizens at that time could not secure that type of insurance protection.[2] The opposition of mutual life insurance companies to savings-bank life insurance presents a unique anomaly. The officials of companies presumably operating for the benefit of policyholders and ostensibly controlled by them spend large amounts of money and much effort to prevent their own policyholders and other prospective buyers of insurance from having access to low-cost, over-the-counter insurance. At any rate, informed consumers in Massachusetts, New York, and Connecticut can increase their insurance protection with less strain on their budgets by making use of savings-bank life insurance.

Foreign Companies. Still another possibility when buying protection is that of dealing with companies organized under the laws of other countries. This involves many questions which cannot be discussed here, but there are some points to be considered to which attention may be called. Two countries whose insurance companies operate in the United States are England and Canada, American Lloyds Associations operating especially in property and marine insurance.[3]

One of the first points to consider is the type of organization, whether mutual, mixed, stock, or individual. Differences in statutory regulation must be examined. For instance, Canadian life insurance companies are permitted to invest a portion of their surplus in common stocks of commercial corporations, a practice which permits larger earnings when business is good but which carries great possibilities of loss even under most expert management. As an illustration one Canadian company was compelled to write off its books as a loss some $2,000,000 worth

[1] TNEC, *Monograph 28*, pp. 164–176.

[2] *Monthly Labor Review*, vol. 50, *Savings-Bank Life Insurance in Massachusetts and New York*, pp. 787–796.

[3] See Straus, Ralph, *Lloyd's; The Gentlemen at the Coffee-House*, Carrick & Evans, New York, 1938, for a description of this unique organization.

of Insull utilities stock in 1932. While it is quite true that American companies had to absorb considerable losses in bad bonds and mortgages, nevertheless most states have limited life insurance company investments to evidences of debt. The Securities and Exchange Commission report suggests that this practice be re-examined with a view to permitting investment in corporate stocks.[1] Are the premiums and benefits of a foreign company payable in American dollars? Does the foreign company have sufficient assets deposited in an irrevocable trust in the United States to meet all liabilities? In spite of efforts to promote peace, war is a factor to be given serious consideration. In the event of hostilities, claims may be canceled and company reserves confiscated, if there is no trust provision. In either case loss results and if the insured should die while his government is at war with the government of the insuring company his beneficiaries may be deprived of protection when they need it most. A similar hazard lurks in the possibility of the government of the insuring company being overthrown, with the successor government repudiating all such claims. That such complications are more real than fanciful is shown by a decision of the New York Court of Appeals, after ten years of litigation, that the Equitable Life Assurance Society of New York need not pay $20,000,000 in claims held by Russians before the establishment of the present Soviet government.[2]

Government Insurance. Except for unemployment and old-age insurance and other minor exceptions, an American civilian consumer cannot buy life, accident, health, or property protection from his state or Federal government at cost. In some states teachers in public schools and all state employees may or must buy protection from the state against old-age dependency. Four years after Massachusetts set up the savings-bank life insurance plan the state of Wisconsin established the State Life Fund in 1911. The law establishing this fund specified that it was to be conducted by the state under the supervision of the Commissioner of Insurance. Participating life insurance policies, the rates and reserves of which were based on the American Experience Table of Mortality and 3 per cent interest, are available to any person of either sex living within the state or a resident at the time the insurance was granted. If an insured person leaves the state subsequently to the purchase of life insurance, policies once in force are not invalidated. The gross annual premium for an ordinary life policy at age 21 is $18.16, but no comparison of net costs can be made, since the dividend record on these policies is not available. Policies may be purchased at home through local offices or by mail. Judged on the basis of the number of policies and the amount

[1] TNEC, *Monograph 28,* pp. 373–374.
[2] *New York Times,* December 31, 1934.

of life insurance in force, the Wisconsin State Life Fund has failed almost completely to meet the purpose for which it was established. After 32 years of operation there were only 1,643 policies in effect for approximately $3,000,000 worth of protection.

During World War I the Federal government went into the life insurance business on a large scale, selling up to $10,000 term insurance to every service man who applied for it. After demobilization the men were permitted to convert their term policies into a permanent form of standard policy. A comparison of premiums on these policies with those of commercial companies shows that elimination of selling and excessive management expenses does benefit the buyer. The government premium on a participating whole-life policy at age 25 was $16.20 per $1,000 payable in monthly installments, as compared with a commercial company rate of $22.10 payable quarterly. This amounts to a difference of 26 per cent in favor of those permitted to buy government policies. It is impossible to compare the net cost of United States Government life insurance with the net cost of a private insurance company policy because none of the private companies offers comparable insurance coverage. All policies issued by the government included provisions granting benefits for total permanent disability for which there is no limit as to the age before which disability must occur. The premiums for combined death and total permanent disability are the net premiums for the death benefit only, calculated for payment on a monthly basis, in accordance with the American Experience Table of Mortality and interest at 3½ per cent. Moreover, there is no loading added to the net premium for expenses, since the government pays all the cost of administration as well as the losses resulting from the extra hazards of the military or naval service.

At the beginning of 1943 there were 589,405 government life insurance policies in force for a total coverage of $2,490,943,114. Only veterans of World War I who have heretofore applied for or have been eligible to apply for war risk insurance or United States Government life insurance are permitted to buy this protection. Civil service employees are not eligible. Any proposal to extend such low-cost protection to citizens generally meets with determined opposition by a few mutual company officials. Such opposition succeeded also in deleting a provision in the original Social Security bill which would have permitted those not included in the old-age provisions to purchase annuities voluntarily from the Federal government at cost.

The National Service Life Insurance Act of 1940 established a new system of insurance for persons who were in active service in the land or naval forces of the United States on October 8, 1940, or who entered

such service after that date. This is referred to as National Service life insurance to distinguish it from United States Government life insurance, which is issued under the World War Veterans' Act of 1924. Both are government insurance but they are entirely separate, each being supported by independent trust funds comprised of premium payments and interest earnings thereon. As of June 1, 1943, there were approximately 9,694,000 applications for National Service Life Insurance, representing an estimated coverage of $68,000,000,000.

On December 13, 1941, the War Damage Corporation was created by the Federal government to provide, through insurance, reinsurance, or otherwise, reasonable protection against loss of or damage to property, real and personal, which may result from enemy attack, including any action taken by the military, naval, or air forces of the United States in resisting enemy attack. The principal office of the Corporation is located in Washington, D. C., and its capital is $100,000,000. As of July, 1943, 4,270,000 holders of War Damage insurance renewed their coverage. The total amount of coverage was $125,000,000,000. Type of claims which had been paid up to that time included damage to insured property resulting from anti-aircraft shells fired at unidentified aircraft; damage caused by a blimp which, returning from patrol duty, went out of control and collided with residences; damage caused by an Army plane which crashed into a college building; damage caused by a plane returning from a patrol mission which accidentally discharged machine gun bullets thereby damaging property; damage caused by a bomber which jettisoned depth bombs too close to shore; and depth bombs dropped by a patrol vessel at sea resulting in property damage on shore.[1]

Actuarial Aspects of Life Insurance

How Premiums Are Calculated. The actuarial aspects of life insurance involve more complicated mathematics than the average layman can understand. But the fact that calculation of insurance premiums is involved is no reason why buyers should not know more than they do about insurance principles and methods. Their very lack of information, often played upon by agents who know little more, gives rise to an air of mystery and a mirage of magic which leads to such fallacies as the belief that "you must die to win" and a naïve faith in the desirability of a 20-year endowment policy.

The selling of insurance policies is a business, which must balance income with expenditures. If a company makes a contract to pay a beneficiary $1,000 upon death of the insured in return for the latter's

[1] *United States Government Manual*, Summer 1943, p. 43; *New York Times*, July 18, 1943.

promise to pay the company, in a lump sum or installments, a price which it sets, there can be no doubt that insofar as actuaries can determine, the price so set will cover the anticipated claim and all administrative costs. How, then, is the price determined?

The starting point is a mortality table. The one used by most American companies is the American Experience Mortality Table, calculated in 1868 on the basis of the mortality experience of the Mutual Life Insurance Company of New York. Such a table pictures "a generation of individuals passing through time." [1] It takes a group of 100,000 from ages 10 to 96, showing the number dying each year. The second step is the application of the law of probability to the mortality table. For instance the probability of death during the ensuing year for men of age 35 is found by dividing the number living at that age, 81,822, into the number who will die during that year, 732. An extension of this principle can be used to calculate the probability of death for 5, 10, 20, or any number of years. Conversely, the law of probability can be applied to the table to ascertain the probability of living for 5, 10, 20, or any number of years. It is on such calculations that annuities are based.

Armed with means for ascertaining the probability of death, the insurance actuary can proceed to quote a price for protection if he knows the age of the applicant, the kind of contract desired, and the maximum rate of interest, probably 3 per cent, which the company is prepared to guarantee. Thus at age 21 the probablity of dying during the next twelve months is .007855 or 7,855 in 1,000,000. By multiplying this decimal by 1,000 the cost of $1,000 worth of protection is found to be $7.85. This can be explained in another way. At age 21 there are 91,914 persons living, of whom 722 will die within the year. If a company were to insure each of the 91,914 lives for $1,000 for a year it would have to charge each policyholder an amount which, multiplied by 91,914, would total $722,000, the known claims. By calculation this sum is found to be $7.85. Similar figures for each age from 21 through 65 are given in Table XXXII.

No account has been taken of interest, but obviously if the premiums are collected annually in advance and if it is assumed that no claims are paid until the end of the year the company will have $1.03 for every dollar collected as premium. Hence $722,000 bears the same ratio to the amount which the 91,914 must pay in as $1.03 bears to $1.00. Dividing $722,000 by $1.03 results in a sum of $700,970.87 which, spread over 91,914 policyholders, requires an annual premium of only $7.62.

[1] HUEBNER, S. S., *Life Insurance*, p. 214, D. Appleton-Century Company, New York. This section is based largely on Huebner's Part II.

All insurance premiums are calculated in this way, with necessary variation for age, type of policy, face value of policy, and method of payment. Nothing will be gained by attempting to explain any of these variations, since any who are interested in pursuing the question further may do so in any standard insurance text.

TABLE XXXII.—AMERICAN EXPERIENCE TABLE OF MORTALITY AND COST OF $1,000 INSURANCE, AGES 22–65[1]

Age	*Number of Deaths per 100,000 Lives*	*Cost of Insurance per $1,000 at Risk*	*Age*	*Number of Deaths per 100,000 Lives*	*Cost of Insurance per $1,000 at Risk*
22	791	$ 7.91	46	1,156	$11.56
23	796	7.96	47	1,200	12.00
24	801	8.01	48	1,251	12.51
25	807	8.07	49	1,311	13.11
			50	1,378	13.78
26	813	8.13			
27	820	8.20	51	1,454	14.54
28	826	8.26	52	1,539	15.39
29	835	8.35	53	1,633	16.33
30	843	8.43	54	1,740	17.40
			55	1,857	18.57
31	851	8.51			
32	861	8.61	56	1,989	19.89
33	872	8.72	57	2,134	21.34
34	883	8.83	58	2,294	22.94
35	895	8.95	59	2,472	24.72
			60	2,669	26.69
36	909	9.09			
37	923	9.23	61	2,888	28.88
38	941	9.41	62	3,129	31.29
39	959	9.59	63	3,394	33.94
40	979	9.79	64	3,687	36.87
			65	4,013	40.13
41	1,001	10.01			
42	1,025	10.25			
43	1,052	10.52			
44	1,083	10.83			
45	1,116	11.16			

But anyone who has bought insurance knows the premiums are higher than this method of calculation will show. Premiums as figured above are known as net premiums, while the rate one pays is the gross premium. The difference involved is fairly large, the net annual level premium at age 21 for $1,000 being $14.72, compared with a gross

[1] State of Wisconsin, Commissioner of Insurance, Forty-Third Annual Report, Part II, *Life and Casualty Insurance*, p. 15. (See text on page 441.)

annual level premium of $19.35, quoted by a mixed company on a participating rate. The difference of $4.63 is the amount charged for expense and compares with $3.44 which is the loading expense of the Wisconsin State Life Fund. The gross premium includes the "loading," a term which covers not only selling, collection, and administrative expenses but also provides a margin for possible contingencies such as errors in net premium due to higher mortality or lower interest yield than expected.

A customary handling of expenses and the loading to cover them includes 80 per cent of the first premium for expenses of securing new business; 10 per cent of renewal premiums for collection expenses; 1½ per cent of the face value of claims to cover settlement costs; ½ per cent a year on assets to pay for expenses involved in making investments; and $1.00 per $1,000 insurance per year for general expenses.

A significant element in modern loading costs is a margin to create a surplus out of which to pay back "dividends"! In the words of a leading authority, "The practice of paying dividends has become so firmly established that the loadings on participating policies are almost invariably made with the further idea of creating a surplus for future dividends."[1] In still plainer language, the buyer of insurance is charged a price higher than the gross cost of the thing purchased in order that officials may return a "dividend," causing policyholders to think that due to good management their net cost of protection has been reduced. This is an evil directly attributable to the mutual company and its principle of sharing costs and benefits mutually according to volume of purchases. On a small scale the mutual plan is excellent but on the scale created by national and international mutuals all mutuality is lost and such a patent hoax as this becomes a national institution, boosting the net annual cost of insurance to a point where many are forced to carry less protection than they should.[2]

[1] HUEBNER, *Life Insurance*, p. 295, D. Appleton-Century Company, New York.

[2] A critical reader of the foregoing paragraph has written that, in his judgment, it is "going a bit too far to treat the dividends paid by mutual insurance companies as an unmitigated 'evil.' The extra funds received in addition to the expected outgo represent something of a cushion which may be used in case future experience becomes unfavorable. If life insurance companies should base their rates on the precise amounts that they expected to pay out, it would mean that, if the experience became unfavorable, and the company were to remain solvent, future policyholders would have to pay excessive rates to make up the deficit on the earlier policies. Without expressing any opinion on the general practices of life insurance companies, it seems to me that you have looked less critically on the statements of the critics than on those practices. The situation has been considerably over-simplified." My criticism of dividends was not a criticism of their use as a cushion but rather a criticism of their use for the purpose of "creating a surplus for future dividends." See pages 446–449 for further discussion of "dividends."

A second significant element which constitutes altogether too large a portion of the loading is the expense for selling, which takes 80 per cent of the first year's premiums and 10 per cent of renewal premiums. The agent who sells a policy is paid from 40 to 60 per cent of the first premium, depending on the terms of his contract, and 5 per cent of the next nine premiums, for a total of practically one full premium. At least one company pays up to 75 per cent of the first premium and several pay more than 50. In some cases, also, the renewal commissions are larger than indicated above. It is this expense which is so much less under the Massachusetts mutual savings-bank insurance plan, enabling savings banks to sell protection for as much as 22 per cent less than mutual companies. The 1929–1939 ten-year average ratio of salaries and commissions to premium income of four insurance companies was 12.02 for ordinary insurance and 20.76 for industrial insurance compared with the ratio of 3.08 of salaries to premium income of Massachusetts savings banks writing insurance. In 1938 the total expenses of Massachusetts savings banks writing ordinary insurance were 8.33 per cent of premium income compared with 13.77 per cent for private companies writing ordinary insurance and 25.45 per cent for "industrial" insurance.[1] There are approximately 192,000 agents in the United States, far more than are needed, collecting this tribute from policyholders. Of the 191,800 persons holding contracts to sell life insurance in the United States in 1940, 69,600 were full-time agents having contracts to write industrial insurance. Of the remaining 122,200 only 50 per cent or about 61,000 were working on a full-time basis. Eighteen per cent were on a part-time basis and 32 per cent held brokers' contracts.[2] In 1938 the Temporary National Economic Committee found 27 leading companies using 24,000 full-time agents who were paid a total gross commission of $20,000,000. Of that sum 82 per cent of the agents received only 30 per cent of the total. Another survey of 35 companies, not including any of the "Big Five," revealed that the largest sum received by any life insurance agent in 1938 was $36,500. The highest average compensation received by agents of 28 companies in 1938 was approximately $3,700.[3]

For life insurance as a whole practically $1,000,000,000 goes for administrative and selling expenses. Life insurance companies have an annual income of $5,000,000,000, of which $3,000,000,000 represents premiums, the remainder being income from interest and rents. Their

[1] United States Department of Labor, *Operation of Savings-Bank Life Insurance in Massachusetts and New York*, Bulletin No. 688, pp. 56–57.

[2] Clark, O. F., *Comparative Services in the Distribution of Ordinary, Industrial and Group Life Insurance*, in McCahan, David, *Life Insurance: Trends and Problems*, *op. cit.*, p. 175.

[3] TNEC, *Monograph 28*, pp. 224–225.

annual expenditures are about $3,500,000,000, of which less than $2,500,000,000 is received by policyholders or their beneficiaries. The Temporary National Economic Committee's analysis of 25 of the largest legal reserve life insurance companies disclosed a total income of $42,680,000,000 during the period 1929 through 1938. During that decade those companies disbursed to policy holders or for operating expenses $32,000,000,000. "This excess of income over disbursements is a notable feature of life insurance companies." It has persisted since 1865. Since 1890 there have been only four years in which total premium income alone for all life insurance companies was not in excess of all disbursements, including payments to policyholders and administrative expenses. In a normal year this excess of income over disbursements runs well over $1,000,000,000 for the 25 leading companies.[1]

Cash Surrender Value. The preceding explanation of how level annual premiums are calculated also explains, by implication, the origin and meaning of the cash surrender value of an insurance contract. To avoid the defect of prohibitive rates with advancing years, characteristic of the natural premiums known as term rates, actuaries have worked out a level yearly charge which exceeds the actual cost in early years by an amount sufficient to offset the deficit in later years. In the case of the $14.72 net premium per $1,000 at age 21 this excess amounts to $6.92. This sum, invested and improved at 3 per cent interest, accumulates a reserve which belongs to the insured and is held in trust for him by the company. If, after the policy has been in effect a few years, the insured finds it necessary to drop his policy because of inability to pay premiums, he has a legal claim to the reserve he has accumulated. Thus an ordinary life policy for $1,000 taken out at age 21 has a cash surrender value of $138 after 15 years. This means that the insured has paid in a sum which, with interest, is $138 more than the actual gross cost of protection during the 15 years. Keeping in mind that the purpose of insurance is to provide protection for dependents in event of premature death, the shortsightedness of cashing in a policy, except in advanced years, should be obvious. On the other hand, the large number of policies surrendered in times of stress is evidence that all too many buyers contract for more insurance than they can afford or, what is more likely, higher-priced insurance than they can afford. In 1932, a severe depression year, there were 15,032,214 policies of all kinds issued by companies reporting to the New York State insurance department as compared with 19,938,725 policies terminated, the latter having a face value of $16,046,985,609. For 1941 the statistics indicate approximately 9,000,000 policies issued, 7,380,000 terminated, with a face value of $8,134,000,000. In the latter

[1] TNEC, *Monograph 28*, pp. 323–324.

year, lapses and cash surrenders accounted for 4,350,000 terminations, while the figure for 1932 was 17,944,000.

Another reason for hesitating to cash in a contract is the common company practice of charging a fee designed to discourage surrender of policies and to cover expenses incident to those surrendered. Some companies charge as much as $25 per $1000 up through the 20th year. In the case of policies surrendered the insured may demand either (1) cash, usually after 90 days, a provision to protect companies during financial panic, or (2) paid-up term insurance, or (3) paid-up insurance of the same kind as the original policy in such amount as the cash surrender value will buy if used as a single premium.

Policy Loans. Similar in origin is the loan value of a policy. Instead of terminating the policy because of inability to pay premiums the insured may borrow from the company the cash surrender value ($138), or part of it, and use the proceeds to pay the next premiums, thus continuing the insurance in force. As security for repayment of the loan the insured must assign the policy to the company, the amount of the loan becoming a first lien on the proceeds of the policy in event of termination.

While policy loans are justified in some cases, they are far too common. For the person who understands the fundamental principles of insurance the policy loan is a legitimate means of securing necessary cash to meet an urgent, temporary need. But the records show that policy loans are frequently the forerunners of lapses. This, of course, is not surprising if the insured is so straitened financially that he is unable to meet his premium payments otherwise. A serious objection to loans on limited payment and endowment policies is that the insured is not only borrowing back his own savings but is paying for them at the rate of 5 or 6 per cent whereas the company credits him with 3 per cent. A final objection to such loans lies in the fact that if the insured dies before repayment the sum going to the beneficiaries is reduced by the amount owed, thus defeating to that extent the very purpose for which the insurance was bought. When insurance buyers generally recognize that they are buying protection, not an investment, there will be fewer policy loans.

"*Dividends.*" There is probably no phase of insurance about which policyholders are more deeply illusioned than the origin and meaning of "dividends." Let it be clearly understood to begin with that the term "dividends" in life insurance is a gross misnomer; that is why the word has been bracketed in quotation marks in this discussion. A more truthfully descriptive phrase would be *surplus sharing*. But what is the origin of the surplus? One clue has been given already. Companies simply

include a percentage in the loading in excess of their already liberal estimates for expense and sometime in the future return that excess percentage to the policyholder. In the words of one insurance expert "some participating premiums are just enough higher than the then current nonparticipating premiums *to give promise of the minimum dividends which would appear seemly to policy holders*."[1] In commenting on the difference in rates between participating and nonparticipating companies, the Securities and Exchange Commission emphasized that the nonparticipating rate is not only adequate but profitable and that there is no reason why the mutual company rates should be so much higher. As a result of such margin mutual companies have extra funds for administrative purposes, enabling them to pay generous salaries and high commissions. "At the same time it enables the companies to pay larger dividends, creating the illusion of very profitable operations, and giving to the policyholder the impression that he is receiving a windfall."[2]

A second explanation is found in the possibility of interest earnings in excess of 3 per cent. In years past companies have consistently earned 4, 4½, or 5 per cent on their policyholders' reserves, yet they have clung to the conservative 3 per cent rate for calculating costs. And perhaps properly so, for recent developments have steadily narrowed the margin to the point where some of the larger companies are put to it to realize much in excess of 3 per cent. A 13-year record of the net interest earnings of the 10 largest companies is shown in the following table:

TABLE XXXIII.—NET RATE OF INTEREST EARNED BY THE TEN LARGEST LIFE INSURANCE COMPANIES, 1928–1940[3]

Year	*Per Cent*	*Year*	*Per Cent*
1928	5.0	1935	3.7
1929	5.0	1936	3.7
1930	5.0	1937	3.7
1931	4.9	1938	3.6
1932	4.7	1939	3.5
1933	4.2	1940	3.4
1934	3.9		

As a result of such declines in interest earnings some companies have lowered their assumed rate of interest to 2¾ per cent or 2½ per cent. A reduction of ½ of 1 per cent in the assumed interest rate is equivalent to an increase of 6 per cent in the gross premium.[4]

[1] RYDGREN, Adolph, "The Significance of Reduced Interest Earnings," in McCAHAN, David, *Life Insurance: Trends and Problems*, *op. cit.*, p. 81. Italics supplied.
[2] TNEC, *Monograph 28*, p. 246.
[3] RYDGREN, Adolph, "The Significance of Reduced Interest Earnings," *op. cit.*, p. 76.
[4] *Ibid.*, p. 82.

A third factor contributing to the surplus is a lower mortality rate than that anticipated. It will be recalled that most companies base their rates on the American Experience Mortality Table which was first published in 1868 and which is based on the mortality experience of one company, the Mutual Life of New York, in the forty preceding years. In spite of developments in public health and the known increase in longevity during the past hundred years, American companies still continue to base their mortality estimates, and consequently their prices for protection, on the mortality records of our ancestors of a century ago. It is small wonder that claims are smaller than anticipated! A glance at the 5-year records of actual as compared with expected mortality for the "Big Five" mutual companies shows a ratio of approximately 60 per cent. The ratio for many companies is much lower, being less than 30 per cent in some cases. The Deputy Insurance Commissioner for Massachusetts is quoted as having testified before a state commission that insurance companies had made more than $1,000,000,000 profit in the years 1934–1937 as a result of their use of obsolete mortality tables based on life expectancy, 1845 to 1860.[1] According to statisticians of the Metropolitan Life Insurance Company, the 1942 expectation of life, based on the records of that company's industrial policyholders, reached a new high figure of 64.18 years in 1942.[2]

Another source of excess surplus has been alluded to and need only be recalled. This is the loading to cover the various costs conveniently lumped under the term administrative expenses. That the surplus for sharing with policyholders could be still larger with drastic reduction in expenses of administration should be evident from what has been said previously.

A final source of income not allowed for is the gain from forfeitures. During the ten-year period 1928–1937, the amount of insurance terminated totaled nearly $127,000,000,000. This was nearly 8 times as great as the increase in insurance in force for the 10 years. Nearly 80 per cent of those terminations were lapses or surrenders. In either case insurance was terminated in a way which did not fulfill the purpose for which it was originally intended. There are no figures showing the losses to policyholders as a result of lapses and surrenders. "Unquestionably this amount would reach staggering proportions if it were known." Gains from lapses and surrenders for all companies during the period 1918 to 1937 amounted to $1,328,000,000 for an average of about $66,000,000 a year. These figures represent fairly accurately the losses

[1] Gilbert, Mort and E. A., *Life Insurance: Investment in Disaster*, p. 59, Modern Age Books, Inc., New York, 1938.

[2] *New York Times*, September 12, 1943, p. 20.

incurred by policy holders. The Temporary National Economic Committee found that lapses and surrenders were due in part to the selling practices used by most insurance companies.[1]

It is from these sources that a surplus is accumulated which may be distributed among policyholders. Contracts sharing in these "dividends" are called participating policies. Nonparticipating policies carry a considerably lower level annual premium, though their net cost in the long run may be higher. For example, the level annual premium quoted by one company for a $1,000 nonparticipating ordinary life contract at age 20 is $14.63 compared with the $19.21 charged by another company for a participating policy. Throughout the ensuing 20 years the buyer of the first contract would continue to pay $14.63, but the buyer of the second policy would receive "dividends" in an amount which would reduce his 20-year average net payment to $13.33. Thus the participating policy with its higher initial cost but lower net cost is discriminatory in favor of the man of means and against the wage earner who needs maximum protection at lowest possible initial *and* net cost. It should be emphasized, however, that the above disparity in net cost is based on a "dividend" history from 1921 to 1941, which may or may not be repeated in the next 20 years. The trend is indicated by the experience of one mixed company. Its current rate for a $1,000 nonparticipating policy is $14.63 at age 20. The company's own "dividend" record for the past twenty years shows an average net premium of $15.29 on participating policies taken out at age 20 for which the gross premium is now $19.00.

As in the case of cash surrender and policy loans, "dividends" may be taken in the form of cash, applied to the payment of premiums, used to purchase more insurance, or allowed to accumulate, building up the individual reserve more rapidly and eventually making a whole-life policy a paid-up contract. In any case, remember that "dividends" are not dividends such as one receives on a business investment; that frequently they are paid from surpluses which should never have been allowed to accumulate to such proportions; and that a portion of them represent nothing more than a return of premiums which should never have been collected.

Optional Settlements. When a policy insuring wealth is terminated by partial or total destruction thereof by occurrence of the event insured against, the usual means of settlement is payment of a cash indemnity, as determined by an appraisal. In some cases the insuring company reserves the right to repair or restore the property at its own expense, if such a settlement is likely to involve less expense.

[1] TNEC, *Monograph 28*, pp. 185–190.

In the case of a claim arising under a contract insuring against sickness or accident, the benefits payable according to the contract are made in cash, upon receipt by the insurer of satisfactory proof of disability. The amount and duration of such indemnities depend, of course, on the terms of the policy.

A life insurance policy, excepting endowment policies, is terminated only by death or by failure to pay premiums. On receipt of proof of death of the insured, the insurer is liable to the beneficiary for the cash equivalent of the face value of the policy, less any loans secured by it. Without in any way abridging that demand claim, the insurer usually offers several optional settlements to the beneficiary, such as the following four. In lieu of cash the beneficiary may elect to receive equal installments of a specified amount, to continue until the proceeds of the policy are exhausted. As a second choice, the beneficiary may elect to receive installments for a specified period, the size of the installments varying, of course, with the length of the period. A third choice available to the beneficiary is that of a life income or annuity equal to the income which the face value of the policy will buy as a single premium for the attained age of the beneficiary. A fourth option is that of leaving the proceeds of the policy with the company at a guaranteed rate of interest, usually 3 per cent, with provision for withdrawal of interest and principal as agreed upon by the beneficiary and insurer.

Which of these options should a beneficiary choose? Frequently, the choice is made by the insured, while living, so he may have the assurance that his beneficiary will be provided for as he wishes. In either case, it may be said that unless there are accumulated debts to be paid at once the insurance should not usually be paid in a lump sum. Most beneficiaries are women unaccustomed to making investments and emotionally unbalanced as a result of their bereavement. Suddenly to receive a check for $10,000 or $15,000 or $20,000 with full responsibility for its investment is to place a burden on the beneficiary which all too often results in tragic loss. One of the important functions of life insurance companies is the investment of funds, and it is usually much the wisest plan for the beneficiary to leave that function to the company, just as the insured did. Moreover, a 1943 ruling of the Treasury Department holds that if the insured makes a request before his death that the proceeds of a life insurance policy be paid in installments, the payments need not be included by the beneficiary in gross income for tax purposes.

With the growing concept of marriage as a partnership, the wise practice which modern families are following is to have a well-qualified insurance counselor advise with the husband and wife. As a result of that consultation the counselor makes an audit of the insured's insurance

estate, including recommendations for terms of settlement. Upon approval by the insured and his beneficiary the counselor then makes the necessary legal arrangements with each of the insurers. There are so many possible desirable settlements, depending on the age of the insured at death, the age of the beneficiary or beneficiaries, the burden of indebtedness, and many other factors, that it is futile even to suggest a typical settlement. The important things are to take time by the forelock and secure the expert, unbiased advice of an insurance counselor to draw up terms of settlement which will yield the greatest benefit to the beneficiary, making periodic alterations as changing conditions require. This need not necessarily involve expense, for increasing numbers of well-trained young agents, particularly those with C.L.U. designations,[1] are performing this service freely as a part of their whole program of selling protection counsel.

Selling Insurance

The Agency Method. Enough has been written to demonstrate effectively that the business of insuring protection against financial loss arising from premature death or any of the other hazards which may befall a family is very complicated—so complicated, in fact, that few of the 50,000,000 to 70,000,000 policyholders understand it. This being the case, it would seem that the business of selling insurance should be restricted to those who do understand it and who bring to their work a professional attitude of service. To what extent does the selling of insurance measure up to this standard? Unfortunately for the millions of buyers there are practically no standards for insurance salesmanship. One standard which dominates this phase of the business and by which the success of an agent is measured is the volume of coverage written. A man or woman need not know anything about the intricacies of insurance to secure an agency contract. A person may have failed in every previous business or professional venture, yet an insurance company may hand him a rate book without any question and tell him to "go to it." The result has been the writing of insurance contracts with an eye to the size of commissions rather than to the needs of the buyer. Frequently these interests are in conflict, but although the insurance agent knows very little about the service he sells, the buyer knows so much less that he proves a gullible victim to the impressive jargon of superficialities.

Responsibility for this situation rests squarely on the insurance companies. The agency-commission basis of selling was adopted about one hundred years ago and continues unchanged. When insurance was new

[1] The College of Life Underwriters is explained in the following section of this chapter.

it had to be sold, and early failures of companies so undermined public confidence in an institution which was not understood that only the most vigorous and aggressive methods were deemed powerful enough to break down sales resistance. That this very policy partially defeated itself by creating disgruntled buyers who failed to get what they thought they were getting was not realized. But that situation has changed. With rapidly increasing emphasis on social as well as private insurance, modern men and women do not need to be sold. But they do need to be guided in their buying by someone who understands insurance and who is professionally concerned with his client's economic welfare. What are the insurance companies of the land doing to provide this new type of agent? Directly, they are doing nothing effective. Most of them give correspondence courses, which are not required, and which still emphasize the technique of selling to an unwilling buyer. Schools of commerce have trained many men in insurance, whom the companies are glad to employ, but for whose training they are in no way responsible.

The Securities and Exchange Commission investigation disclosed that only 29 per cent of the companies surveyed require their agents to have preliminary training before going out for solicitation. Most of the training courses are very short. The seven companies whose training courses are fairly complete and the ones definitely most advanced in preparing their agents are Acacia Mutual, Aetna, Bankers' Life (Iowa), Connecticut Mutual, Northwestern National, Penn Mutual, and Southwestern Life. The Commission concluded that

> "Economic and management pressure on the agent to sell more and more life insurance must be reduced and in substitution thereof must come a willingness on the part of life insurance company managements to discard 'growth for growth's sake alone' in favor of a selling program which has as its primary objective the sale of insurance in the manner which is most suitable to the policyholders' needs and their ability to pay. The unfit agent must be eliminated and only those persons equipped through careful selection and training to approach the public in a professional manner with a view to rendering expert service must be permitted to carry a rate book for a legal reserve life insurance company. Unless these things are done immediately through the combined effort of regulatory officials and company managements, the time will have arrived when the social disadvantages resulting from the system as presently conducted can no longer be ignored."[1]

The American College of Life Underwriters was organized to raise insurance salesmanship to a professional level. It gives no courses but

[1] TNEC, *Monograph 28*, pp. 212, 214, 234.

does conduct examinations for candidates who have studied in college, or independently. Its examinations are based on the assumption that the efficient underwriter needs a broad business education, including some knowledge of economics, government, sociology, taxation, corporation finance, banking, investments, and law as it pertains to insurance, commerce, wills, trusts, and estates. In addition to this broad training he must be thoroughly versed in his own field. If you do not mind embarrassing the next agent who approaches you, measure his ability by that standard. Successful completion of examinations is rewarded by a C.L.U. (Chartered Life Underwriter) designation. While insurance companies like to have C.L.U. men and women as agents it is usually because they expect more business, not because they insist upon better insurance service. At the end of ten years there were 1,237 men and women who had passed the C.L.U. examination. Not only is this a very small proportion of the 191,800 agents writing life insurance, but it is found that there were only 17 companies which numbered 20 or more C.L.U.'s among their agents. Northwestern Mutual, Equitable Life (New York), Massachusetts Mutual, Mutual Benefit Life, Prudential, and Penn Mutual, were the only six companies having 50 or more.[1] It is still true, as it was when our grandfathers bought insurance, that anyone is allowed to sell. Until the time comes when companies restrict their agency contracts to persons who are required to prove their qualifications for advising clients on their insurance programs by passing a creditable examination, or until the various states require the passing of examinations comparable in standard to medical and bar examinations, the wisest procedure for buyers is to insist that anyone seeking to sell them life insurance must possess a C.L.U. designation or be working toward that goal. Then, and only then, will the millions of insurance buyers receive the kind of protection counsel which they have every right to expect.

Buying Insurance

A Summary of Procedure. The purpose of this chapter, together with the one preceding, is to outline, for prospective buyers of protection, the nature and basic principles underlying insurance; to present the main differences in types of policies and types of companies issuing them; to explain the actuarial aspects of premiums, cash surrender values, policy loans, and surplus sharing; and finally to help buyers

[1] Woods, Lawrence, Jr., C. L. U., *The First Decade 1927–1937, A Brief History of The American College of Life Underwriters*, published by The National Chapter, Chartered Life Underwriters. For further information address The American College of Life Underwriters, 36th and Chestnut Sts., Philadelphia, Pa.

determine the qualifications of agents who hope to sell them insurance. There is one final recommendation to offer as a guide in developing qualities of "buymanship." In order to achieve a well-balanced insurance estate one must first determine his needs. One's personal insurance program must include provision not only for dependents in case of premature death, but should include also provision for loss of income resulting from accident or sickness or old age. One's property insurance program should include protection against loss by fire of one's house, household goods, and automobile. Automobile owners also need public liability insurance, theft insurance, and, if it can be afforded, property damage insurance.

Much more has been written about life insurance in these chapters than about the other forms, not only because the purchase of life insurance involves many complex problems, but because the amount of money invested throughout the years is considerably larger than for the other forms of protection. Certainly one's personal insurance program covering premature death, accident, health, and old age involves far greater expenditures than does the property insurance program of the average middle-income consumer.

Having ascertained one's needs, the next step is to determine which types of contracts will fulfill those needs. The third step is to decide which type of company is best suited to write the policies needed, at the lowest net cost. It is at this point that one must turn to agents. One should not wait for the most aggressive agents to call, but rather should ask the nearest branch office of each type of company to have its best C.L.U. representative call. These men should be given the necessary information as to income, liabilities, and family responsibilities, and each one should be asked to work out what he regards as the strongest insurance program commensurate with the prospective buyer's ability to pay. Each should be asked to submit with his proposals a written statement setting forth the type of company he represents, its size as measured by assets and number of policyholders, the state in which it is chartered, its ratio of management expense, and such other information as one may want. After comparing the arguments of all the agents and canceling out those found unreliable, one should go to the nearest public library or write to the Insurance Commissioner of the state which chartered each of the companies for a copy of the latest report on its comparative condition.[1] With all this information one should then be able to choose the program and the company whose contracts best meet one's needs.

[1] A convenient source of such information is the *Little Gem Life Chart*, published by the National Underwriter Company, 420 East Fourth Street, Cincinnati, Ohio. Its price is $2.50.

The authors of *Monograph 28* conclude that "since the financial strength of the principal American life insurance companies . . . is in most respects on a par . . . the relative costs of . . . insurance should become the most important consideration when . . . purchasing life insurance."[1] The next and final step will be to work out with the beneficiary, with the aid of one of the agents in whom the insured has confidence, the methods of settlement which will assure to dependents the protection he is seeking to provide. That done, one may face the uncertain future with greater confidence in the knowledge that he has done all in his power to discharge the obligations owed by a man to his family and to society.

QUESTIONS FOR DISCUSSION

1. Is a mutual insurance company a consumers' co-operative?
2. If you were buying a life insurance policy now would you prefer to deal with a mutual or with a stock company?
3. Why do you suppose mutual life insurance companies so completely dominate the field in the United States?
4. If the Federal government can regulate the securities markets why can it not regulate insurance companies?
5. How does the Massachusetts plan of mutual savings banks life insurance compare with a co-operative? With a stock company? With the New York plan?
6. Would you favor authorizing the Federal government to sell life insurance to all civil service employees? To all citizens?
7. Explain how a life insurance premium is calculated.
8. Is it ever advisable to borrow on one's life insurance? Why is it possible?
9. How do insurance "dividends" differ from the dividends of a business corporation?
10. Would you favor a plan of selling life insurance over the counter through branch offices?

PROBLEMS AND PROJECTS

1. Compare the number of policies, and the volume of business, written by stock, mixed, and mutual companies writing life insurance in your county.

2. Apply the procedure in problem 1 to stock and mutual fire insurance companies.

3. Secure a copy of your state insurance laws. Examine them carefully. Are they rigid or lenient? Are they well or poorly enforced?

4. Write to the Insurance Commissioner of New York State for a copy of his last annual report and summarize it for the class.

[1] TNEC, *Monograph 28*, p. 238.

5. Write a report on the Massachusetts plan of savings-bank life insurance.

6. Prepare a paper on the operation and probable future development of Federal government life insurance.

7. Undertake a field study of your county to discover how many agents are licensed to sell life insurance there. What training have they had? How many have C.L.U. designations?

8. Does your state require prospective life insurance agents to pass an examination? If not, what reasons can you find; if so, secure a copy of the questions and analyze them in class, answering as many as you can.

9. Review Gilbert, Mort and E. A., *Life Insurance: Investment in Disaster*, or McCahan, David, (Editor), *Life Insurance: Trends and Problems*, or TNEC, *Monograph 28*, *Study of Legal Reserve Life Insurance Companies*.

22

Buying Shelter: To Own or Rent

The Consumer Shops for Shelter

Shelter Is a Necessity. Next to food, protective shelter from the elements is the greatest need of consumers. Regardless of climate, people everywhere have need for housing. Favorable climate may render clothing unnecessary, but protection from heat or cold, rain or snow, wind, animals, and insects is essential. People may live comfortably and happily without many of the comforts and luxuries of modern civilization, but without shelter of some kind they cannot live at all.

Statistical evidence demonstrates the importance of shelter in the business of living. A survey of family expenditures in 1935–36 showed American families spending $40,843,000,000 for all consumption items. The largest single item was food, for which $13,713,000,000 was spent, representing 28.8 per cent of the total income and 33.6 per cent of total consumer expenditures. Ranking second in importance was the $7,287,000,000 spent for housing, representing 15.3 per cent of total income and 17.9 per cent of total consumer expenditures. The third largest item was that for household operations, amounting to $4,764,000,000, representing 10 per cent of total income and 11.7 per cent of total consumer expenditures.[1] Lumping these three items together it is found that in 1935–36 American families spent 63.2 per cent of their total consumption outlay for food, housing, and household operations.

Figures for family expenditures and consumption items take on greater meaning if they are broken down according to income levels. That quarter of American families having the lowest incomes, under $710, spent 23.6 per cent of their incomes for housing; the second quarter, with incomes from $710 to $1,160, spent 18.4 per cent; the third quarter, having incomes of $1,160 to $1,840, spent 16.9 per cent; the top quarter, with incomes of $1,840 and over, spent 12.8 per cent of their income for housing.[2]

It is helpful also to compare the housing expenditures among farm, rural nonfarm, and urban families. The following table shows these comparative expenditures by income groups and by type of community.

[1] National Resources Planning Board, *Family Expenditures in the United States*, p. 23, U.S. Government Printing Office, Washington, 1941. [2] *Ibid.*, p. 46.

TABLE XXXIV.[1]—AVERAGE EXPENDITURES FOR HOUSING OF FARM, RURAL NONFARM, AND URBAN FAMILIES AT SELECTED INCOME LEVELS, 1935–36

Income Level and Type of Community	*All Housing*	*Income Level and Type of Community*	*All Housing*
$500–$1,000:		$3,000–$4,000:	
Farm	$ 82	Farm	$319
Rural nonfarm	136	Rural nonfarm	382
Urban	186	Urban	538
$1,500–$2,000:		$5,000–$10,000:	
Farm	197	Farm	488
Rural nonfarm	236	Rural nonfarm	510
Urban	323	Urban	963

Regional differences in average expenditures of American families for housing are shown in the following Table XXXV. As might be supposed, the average expenditure for housing by families in New England

TABLE XXXV.[2]—AVERAGE EXPENDITURES FOR HOUSING OF ALL FAMILIES AND OF FARM, RURAL NONFARM, AND URBAN FAMILIES IN FIVE GEOGRAPHIC REGIONS AT SELECTED INCOME LEVELS, 1935–36

Income Level and Region	*All Families*	*Farm Families*	*Rural Nonfarm Families*	*Urban Families*
$500–$1,000:				
New England	$ 204	$155	$197	$ 209
North Central	182	142	150	207
South	81	43	104	127
Mountain and Plains	155	132	156	196
Pacific	162	117	153	182
$1,500–$2,000:				
New England	313	256	300	319
North Central	313	234	230	344
South	231	135	221	278
Mountain and Plains	259	179	264	306
Pacific	257	201	230	275
$3,000–$4,000:				
New England	513	280	439	569
North Central	518	327	364	553
South	453	324	392	513
Mountain and Plains	427	241	371	523
Pacific	431	327	335	472
$5,000–$10,000:				
New England	1,140	446	698	1,126
North Central	813	324	395	1,007
South	649	475	562	819
Mountain and Plains	621	515	380	879
Pacific	788	858	601	766

[1] *Ibid.*, p. 10. [2] *Ibid.*, p. 15.

is higher than in other regions, while the average expenditure for families living in the South is less for those families having incomes below $3,000.

What Does the Market Offer? In view of the preceding discussion and figures it might be concluded logically that the business of constructing houses is one of the largest and most important of all economic undertakings. The total number of dwelling units in the United States in 1940 was 37,325,470. Of that number 21,616,352 were urban, 8,066,837 were rural nonfarm, and 7,642,281 were rural farm. Of the total number of dwelling units, 34,854,532 were occupied at the time the census was taken. Of that number 43.6 per cent were occupied by owners, and 56.4 per cent were occupied by tenants.[1]

The median age of dwelling units in the United States was found to be 25 years.[2] The median number of rooms for the country as a whole was 4.73. Although 34.7 per cent of the houses had more than 5 rooms, 26.6 per cent had fewer than 4 rooms. Homes occupied by their owners had on the average $1\frac{1}{2}$ more rooms than those occupied by tenants and, measured by the number of persons per room, were less crowded than those occupied by tenants.[3]

Nearly two thirds of all families in the United States live in one-family detached structures. The precise figure was 63.6 per cent. As might be supposed, the percentage was much higher in rural farm and rural nonfarm areas.[4]

The median size of households in the United States was 3.28 persons in 1940. There is little difference in this respect among urban, rural farm, and rural nonfarm areas, the figures being 3.16, 3.81, and 3.21. Practically 55 per cent of the households numbered one, two, or three persons, while those comprising four or five persons constituted approximately 30 per cent of the total, and those with six or more 15 per cent. It was found that home owners in urban areas tended to have larger households than tenants, but in rural areas tenants' households were larger than those of owners.[5] The number of new dwellings constructed from 1930 to 1940 was much smaller than the number built from 1920 to 1930. The average annual volume of 850,000 units during the latter period compared with average annual construction of 550,000 units constructed in the period of 1930 to 1940.[6]

The median monthly rental of homes in the United States in 1940 was $27.31 in urban areas, $13.20 in rural nonfarm areas, and $5.97 in rural farm areas. These figures include the monthly contract rent paid

[1] United States Department of Commerce, Bureau of the Census, *Sixteenth Census of the United States, 1940: Housing*, p. 3.

[2] *Ibid., Series H-13*, No. 13.

[3] *Ibid.*, No. 7.

[4] *Ibid.*, No. 10.

[5] *Ibid.*, No. 8.

[6] *Ibid.*, No. 13.

by tenants and the estimated monthly rent of owner-occupied and vacant homes. Although there was not much difference in rent as between the North and the West, rentals in both those regions were substantially higher than in the South. The median rent of urban and rural nonfarm homes was $26.69 in the North, $24.22 in the West, and $13.83 in the South. Similar figures for rural farm home rentals in the three areas were $11.26, $9.07, and $3.92.[1]

When a young married couple set forth to rent, buy, or build a house, what does the market offer them? This is a question with thousands of different answers. Living quarters ranging from palatial residences to slums unfit for human habitation await these newlyweds. There is no such thing as an average American home. Although in normal years $1,500,000,000 is spent on residential construction and $1,000,000,000 is spent on repairs and remodeling, persons in the lower-income groups find a supply of miserably inadequate tenements or undesirable houses and apartments priced beyond their income. A substantial proportion of the 37,000,000 dwelling units in the United States are obsolete or substandard. It was found that nearly half of these units—49.2 per cent—in 1940 were in need of major repairs or lacked private toilet facilities. Structures were classified as needing major repairs when floors, roofs, plaster, walls, or foundation required repairs or replacements, the continued neglect of which would impair the soundness of the structure and create a hazard to its safety as a place of residence.[2]

In 1940 there were 4,503,000 more families in the nonfarm areas of the United States than in 1930, yet only 2,734,000 housekeeping units had been built in that ten-year period. That left 1,769,000 families who were required to make their homes in other than new housekeeping units. About 908,000 of them lived in residential structures which had been erected before 1930. The remaining 861,000 families had to double up or find living quarters in other types of shelter. Automobile trailers became the permanent homes of 100,000; 416,000 established their households "in the back of stores, in public buildings, warehouses, garages, shacks, houseboats, barns, tents, boxcars, caves, dugouts, and in other such places claimed as residence on enumeration day."[3]

Costs of construction vary widely throughout the country. The cost of building a house of identically the same form and materials in 27 cities in 1935 was found to vary from 18 cents a cubic foot in Columbia, South Carolina, to 26.8 cents in Providence, Rhode Island. This house, classified as a $6,000 structure (though varying from $4,320 to $6,432),

[1] *Ibid.*, No. 11.
[2] Census of the United States, 1940, *op. cit.*, *Housing*, First Series, pp. 4–5.
[3] *Monthly Labor Review*, vol. 54, p. 870.

provides 24,000 cubic feet of living space. This is divided among living room, dining room, kitchen, and lavatory on the first floor, with three bedrooms and bath on the second. It includes an open attic and a one-room cellar containing heating and laundering facilities. The exterior finish is of wide board siding with brick and stucco. A one-car garage is attached to the side of the house. It is significant to note that this $6,000 house does not include a gas range, hot-water heater, window screens or shades, lighting fixtures, interior decorations, or land.[1] Such housing is far beyond the reach of a worker, 20 per cent of whose income would permit him to pay a monthly rental of not over $23.50. This is equal to only $6 a room for 3½ rooms. In order to rent or buy such a house the average worker would have to spend some 40 to 60 per cent of his income for shelter.[2]

The wide variation in residential values is shown in Table XXXVI. These differences reflect "underlying economic, social, and physical

TABLE XXXVI.[3]—REGIONAL DIFFERENCES IN VALUES OF NONFARM DWELLINGS, 1930

Region	*Average Value of*			*Relative Value of*		
	All houses	Owner-occupied houses	Rented houses	All houses	Owner-occupied houses	Rented houses
United States	$5,022	$5,833	$4,347	100	100	100
New England	4,885	6,748	3,467	97	116	80
Middle Atlantic	7,025	7,824	6,759	143	134	155
East North Central	5,376	5,927	4,803	107	102	110
West North Central	3,549	4,253	2,765	71	73	64
South Atlantic	3,397	4,883	2,406	68	84	55
East South Central	2,712	3,846	1,960	54	66	45
West South Central	2,967	3,712	2,412	59	64	55
Mountain	2,886	3,259	2,547	57	56	59
Pacific	4,918	5,765	4,169	98	99	96

differences arising from climate, unequal natural resources, varying degrees of industrial and agricultural development, differences in income and the expense of urbanization, as well as local custom and tradition. In dealing with dollar values it is not possible fully to show qualitative differences, and the regional values given here represent comparable housing facilities only in part." Site value is an important factor in determining differences in the value of residential property. It con-

[1] *Monthly Labor Review*, vol. 42, p. 647. [2] *Ibid.*, vol. 38, p. 625.

[3] Based on WICKENS, David L., *Differentials in Housing Costs*, National Bureau of Economic Research, Bulletin 75, 1939.

stitutes 20 per cent of the value of older property and 15 per cent of the value of new property. Houses in the New England and Middle Atlantic states are predominantly of brick construction, which costs more than frame houses. Other factors affecting the relative rents and values are the absence or presence of facilities, community services, age, availability of credit, differences in costs of material and labor.[1]

To the extent that private residential living quarters were constructed, the dwelling units were not provided at a cost which placed them within the reach of families in the low-income group during the decade 1930–1940. It is estimated that in 1938, 81 per cent of the new single-family houses were valued at $4,000 or more. Taking such property as the level below which new housing facilities become available to families with income of $2,000 or less, it is found that more than four fifths of the new properties were too expensive for more than four fifths of the families in nonfarm areas.[2]

That something is wrong with the business of providing people with shelter is evidenced by the perennially large number of politico-economic experiments in providing low-cost housing. In one area where dwellings were being erected by the United States Housing Authority, the average net construction cost was $2,830 per home. For private construction the average valuation for each dwelling unit was $3,800. The total costs of providing a new home for a family living in the slums, including dwelling facilities and the cost of land, averaged $4,507 per home.[3]

Philadelphia is well known as a textile manufacturing center, and Philadelphia hosiery workers are well organized. According to prevailing standards they are well paid also. What sort of housing do they have, and what does it cost them? A survey of 1,400 families revealed an average weekly wage, of those who received any income at all, of $26.75 per family. Out of 1,354 families 23 per cent owned their homes free of all encumbrance, 43 per cent owned homes which were mortgaged, while 29 per cent rented their living quarters. The percentage of home ownership is definitely larger in the older-age group. Among 1,127 families over thirty years of age 70.5 per cent owned their homes. The average cost of these homes was $5,720, 42 per cent of the cost price being covered by mortgage. Taking 10 per cent as the minimum cost of carrying and maintenance, the monthly expense to these homeowners would be $47.60, compared with an average rental paid by nonhomeowners of $28.35 a month.[4] Perhaps it should be noted also that the latter group have nothing to lose in depreciation and are less tied to a particular job.

[1] *Monthly Labor Review*, vol. 49, pp. 1094–1097.
[2] *Ibid.*, vol. 49, p. 879.
[3] *Ibid.*, vol. 48, pp. 1084, 1085.
[4] *Ibid.*, vol. 37, p. 627.

A later survey of all Philadelphia families, made by a private mortgage corporation, revealed that the average family in that city seeking a low-cost home has an income ranging from $1,080 to $1,500. This means that they cannot pay more than $25 a month for rent, or for carrying charges on the purchase of a home. Breaking the families into groups it was found that 41 per cent had incomes of $1,200 annually or less and that an additional 33 per cent had incomes ranging from $1,200 to $1,500 annually. The remaining quarter had incomes of from $1,500 to $2,500. The rents being paid at the time of the survey ranged from $20 to $40 a month with an average of $29.78.[1]

Clearly the cost of housing in relation to family income is too high. Also the cost of housing is too high as compared with other things. As a consequence the number of families owning their homes has been declining. In 1930 approximately 48 per cent of the dwelling units were owned, as compared with 52 per cent which were rented. In 1940 only 44 per cent of the occupied dwelling units were owned, as compared with 56 per cent which were occupied by tenants.[2] The ratio of cost of home ownership to family income is from 1½ to 3 times a year's income. For incomes ranging from $2,100 to $4,800 a year the ratio is 1.9. This means that a family with an income of $2,100 cannot afford to own a home costing more than $3,990, nor a family with an income of $4,800 a home costing more than $9,120. And a family receiving an income of $1,800 cannot afford to spend more than $3,150 for a home.[3] This situation creates a strong tendency to purchase dwellings beyond financial means, which in turn results in considerable loss.

The 1940 Census revealed a median monthly rental of $27.31 for homes in urban areas, a figure equal to an annual rent of $327.72, as compared with the $300 which Bemis thinks is the maximum for wage earners. If 14 per cent is taken as the annual cost to the nonoccupying owner, persons with $300 to spend for shelter could not afford to rent houses costing much more than $2,000. Yet, as already shown, the average cost of building new houses is in round numbers from $4,000 to $5,000.[4]

The Backward Art of Home Building

Static Styles in a Dynamic Age. There has been no significant advance in the art of building houses in the past 300 years, yet tremendous changes have occurred in the production of practically all other economic

[1] *New York Times*, January 22, 1940.

[2] Census of the United States, 1940, *Housing*, First Series, p. 4.

[3] Bemis, Albert Farwell, *The Evolving House*, vol. 2, p. 395, The Technology Press, Massachusetts Institute of Technology.

[4] *Ibid.*, pp. 112, 132, 133.

goods and services. The medical profession has adapted new discoveries in the field of science; manufacturers similarly have adapted new developments in the technique of living; but houses of today are built in essentially the same way as those occupied by our colonial ancestors. The Industrial Revolution introduced a fundamentally different method of producing goods. The Machine Age has created mass production at low cost. Yet these very methods of large-scale production so beneficial in other lines have not been adapted to such a major industry as that of constructing dwellings.

The power of custom is clearly evident. As in colonial days when timber was abundant and other types of building materials were either too expensive or unknown, the typical house of today is a wood-frame structure. It is very largely devoid of fireproofing, insulation, or other adaptations to meet twentieth-century changes. Among recent developments are the reduction in the size of families and the increasing concentration of people in towns and cities. The average number of persons per family has diminished from 4.9 in 1890 to 3.8 in 1940. Yet the typical house is a large, rambling, poorly arranged structure. Three fourths of the population live in old-style, one-family houses and such attempts as apartment building to meet the problem of housing city dwellers have shown but little adaptation to technical improvements developed in other lines.[1]

New Wine in Old Bottles. "We are clearly putting new wine into old bottles when we implant modern heating, lighting and plumbing into the house structure and architecture of two centuries ago."[2] Instead of the modern structure being adapted to modern housing conveniences, the reverse process has taken place. Old frames are renovated and modernized by laying hardwood floors on top of wide pine boards, by converting an ill-adapted catch-all room into a bathroom, by excavating a hole in the ground to provide space for a furnace, by defective wiring for electricity to replace the former method of lighting by gas. Though modern science has failed to produce low-cost houses on a large scale it has produced an amazing array of housing accessories and appliances. In 1940 seven out of ten dwelling units in the United States were equipped with running water and six out of ten had a private flush toilet in the structure. More than 56 per cent of the 37,000,000 homes had a private bathtub or shower. More than 14,000,000 of the 37,000,000 had central heating plants and more than half of the homes in the United States had gas or electric cook stoves. Nearly 77 per cent of the dwelling units had electric lights and 44 per cent had mechanical refrigerators. From 1930 to 1940 the number of American homes with radios more than

[1] Bemis, *op. cit.*, vol. 2, p. 37.

[2] *Ibid.*, *op. cit.*, vol. 1, p. xi.

doubled, the percentage in 1940 being 83 compared with 40 per cent in 1930.[1] American ownership of 32,500,000 automobiles not only required storage facilities but resulted in greater freedom for city dwellers to live in outlying sections and for those of the country to reach town or city with greater ease.

Why Are Houses Expensive? What are the reasons for the high cost of building? Why is it that occupants of old-style houses think they cannot afford better homes yet feel they can afford a complete line of modern home accessories? Answers to these questions are extremely complex. Among other explanations they include the following.

Among general causes, the localized nature of the construction business is one reason for excessive cost. Even yet the customary procedure in building a house is to gather materials at the building site, where the house is manufactured. In 1938 it was reported that 74,800 builders constructed 166,900 urban one-family houses. Only 6,600 of these builders constructed five or more houses.[2] In contrast with this method the automobile industry manufactures the various parts in one large factory and they in turn are assembled into complete units in widely scattered assembly plants. Just as this method reduces costs of automobile manufacture, so the failure to use it so far as possible in house manufacturing results in higher costs. In 1935 and 1936 a number of companies set out to develop the pre-fabricated house, fully equipped with such improvements as air conditioning, oil heating, and modern insulation. Prices varied from $2,500 for a four-room frame house to $3,800 for a four-room steel house. A six-room house was quoted at $4,500, including lot. As a result, an insufficient number of dwelling units was constructed in the decade 1930–1940, resulting in an acute housing shortage as the United States launched into a defense economy and soon after into a war economy. It was imperative that the Federal government assist in providing living quarters in certain areas. Time was short, as a result of which emphasis was placed upon pre-fabrication. One such structure was described as a demountable house. A typical unit included two bedrooms, a living room, and a kitchen at a cost ranging from $2,500 to $3,000. The cost for demounting and re-erecting these houses ranged from $250 to $550.[3] By 1942 88,000 demountable pre-fabricated units had been constructed.

It is estimated that there will be a total annual demand for 600,000 new houses when the nation resumes a peacetime economy. With this

[1] Census of the United States, 1940, *Housing*, Series H-13, Nos. 12, 5, 6, 3, 2, 4, 1.

[2] *Monthly Labor Review*, vol. 52, p. 1283.

[3] Reed, William G., *Prefabrication and the Defense Housing Boom*, National Housing Agency, Washington, D. C., 1941.

prospect in view, and with the stimulus provided by the Federal government for pre-fabricated structures in defense areas, many firms in 1943 were looking to the future. Within the building industry it is estimated that there were then more than 300 companies operating and preparing to build pre-fabricated houses on a large scale in the postwar period. One firm had already made arrangements to sell its houses through a chain of department stores. The average cost for all types of such houses was estimated at $700 a room up to six rooms, after which the cost jumps to $900. These prices, of course, are based on the 1943 price level.[1]

A survey of 200,000 consumers to discover their preferences in residential construction revealed some surprising results. In spite of much advertising of modernistic houses, it developed that consumers remain conservative in their wants. They rejected electric unit heaters, ground-floor utility rooms, and kitchenettes. It was concluded that there would be no revolutionary changes in house construction or design, and that the immediate postwar small house would be practically identical with its 1941 prototype, with a few accessory changes to add novelty and to give an appearance of modernism.[2]

The building industry is not well organized. It consists largely of a loose collection of related crafts. When a person lets a contract for construction of a dwelling, the general contractor immediately lets out numerous subcontracts for heating, electrical work, roofing, painting, and other such specialized tasks. This work is frequently done by individual craftsmen who fail to use modern machines and methods. Co-ordination in their activities is largely a matter of chance. After a carpenter has completed his work the plumber finds it necessary to bore holes for his pipes, and the heating contractor rips out portions of walls and floors for hot- and cold-air vents.

As in so many other industries, there is excess capacity. Facilities for building homes are 30 per cent greater than would be needed if demand were uniform. Overhead costs on this excess capacity increase all costs of construction.

For many years building construction was considered absolutely seasonal. As a result of modern developments, engineers contend that construction work can be carried on in winter as well as in summer; in fact, there are some who claim that costs of construction are lower in winter. Yet the industry as a whole is still definitely committed to the practice of seasonal construction, which adds to its cost.

For the most part houses are custom- rather than factory-built. This is partly due to failure of the industry to develop factory methods,

[1] *Tide*, June 1, 1943, pp. 13–15; *New York Times*, April 17, 1943.
[2] *Business Week*, September 11, 1943, p. 17.

and partly due to an insistence by homeowners upon what they choose to call individuality. Persons who are perfectly satisfied to ride in a standardized automobile, to listen to a standardized radio, and to preserve food in standardized refrigerators insist that they will not live in a standardized house. Much of this so-called individuality occurs in places where it is seldom seen. For example, there are about 600 different styles and sizes of window sash. This offers a great range of choice for individualists, but at the same time it increases the cost of their homes.

There are many hazards involved in building a house. Adequate insurance against them may increase the total cost of construction by as much as 7 per cent.

The architectural profession is not properly appreciated nor fully developed. The usual architectural fee is 4 per cent of construction costs. As a result probably 80 per cent of single-family dwellings are built without the services of an architect. In many cases this represents a pinchpenny philosophy of economy. On the other hand, architects are largely bound by tradition which operates to retard any increasing use of standard specifications. The practice of securing competitive bids among architects and builders is estimated to increase building costs by 3 per cent.

In certain of the larger cities the building trades are among those most thoroughly organized by workers. From the prospective builder's point of view, the difficulty here lies in the fact that unionization has developed along craft rather than industrial lines. This results in frequent jurisdictional disputes; the members of one union, for example the carpenters, will contend that a particular part of the work should be allotted to them, while the members of another union, perhaps the metal workers, will contend that the work falls within their jurisdiction. No matter to which union the work is given, the other may precipitate a strike which ties up activities and increases costs. Because of the seasonal nature of the building industry there has been a strong tendency for unions in the building trades to follow the policy of restricting output. Bricklayers' unions will specify the maximum number of bricks which may be laid in a day, while painters' unions will set the maximum width of brush which members may use.

For the average consumer the construction or purchase of a home involves a large capital investment. In most cases it represents probably the largest single expenditure the family will ever make. Moreover, very few are able to pay cash. This means they must borrow, thus increasing the total cost. Difficulties in costs of financing are given special treatment in the next section of this chapter.

As population has increased, the necessity of protecting other property owners has resulted increasingly in building-code restrictions. While these probably do not affect residential construction as much as apartment houses, office buildings, and other business structures, they do raise costs to some extent. For generations cities and states have raised from 60 to 90 per cent of their revenue by taxing land and buildings. The percentage of rental absorbed by taxes varies among states from 16 to 34.5. This operates frequently to discourage construction of buildings for sale or rental.

Consumers themselves are responsible to some extent for the high cost of houses. Even though purchase or construction of a home is often the largest single investment a buyer makes, requiring from one sixth to one fifth of his income for maintenance, his decision is based on a woeful lack of knowledge. The average buyer knows no more about the details of the house he buys than he does about the mechanical operation of his radio or automobile. There are numerous ways in which profit-seeking builders can cut costs and yet produce a house which is outwardly well-built and attractive. Yet within a year many owners find that, as a result of shoddy construction, maintenance and repair costs are greater than they anticipated. It is a commonplace among building contractors that a $75 gadget will sell a $7,500 house. Women buyers are easily influenced by such devices as laundry chutes, folding ironing boards, or black-tile bathrooms.[1]

Financing the Purchase of a Home

Installment Buying Is Common. Because of the large investment, one of the first fields in which installment buying developed was that of home purchase. For the country as a whole, probably half the homes owned by occupants have been bought on credit. One study of 918 homes showed that 96 per cent were built on credit. First mortgages covered approximately 53 per cent of the total cost, while second mortgages covered up to 28 per cent. This means that about 80 per cent of the purchase price was supplied on credit.[2] These figures are verified by those resulting from the study of home ownership among Philadelphia hosiery workers (page 462). It will be recalled that 43 per cent of the 1,354 families owned homes which were mortgaged up to an average of 42 per cent of their total value. Of the 11,413,000 dwelling units in the United States occupied by their owners in 1940, 45 per cent were mortgaged. Mortgage statistics on one-family nonfarm houses built from 1935 to 1940 show an average value of $5,019 and an average mortgage

[1] For an elaboration of these points see Bemis, *op. cit.*, vol. 2, chap. 4.
[2] *Ibid.*, p. 348.

debt of $3,125, equal to 62.3 per cent of the value. These mortgages were held by building and loan associations, commercial and savings banks, life insurance companies, mortgage companies, and individuals.[1]

There are three main elements in housing cost. The first of these is land, which, including improvements, accounts for approximately 20 per cent of total cost. The building itself, including materials, labor, builder's overhead and profit, accounts for about 70 per cent. The third main element is financing cost, which covers interest, commissions, and discounts on loans, or approximately 10 per cent of the total. In those cases where architect's services are used, the fee amounts on the average to 4 per cent, with an additional 2 per cent if the architect is responsible for supervision of the work.[2]

Financing Methods and Costs. The most common agencies for providing credit for home purchase are building and loan associations, insurance companies, and savings banks. Building and loan associations are banks organized on the co-operative principle. In order to secure a loan, borrowers must become members of the association. They subscribe for shares of stock, paying for them by means of a fixed sum in the form of monthly dues. Interest is paid on these installments, and penalties are inflicted for delinquency. Upon completion of payments, members are entitled to the face value of their shares, which commonly amount to $200 each. Many members use these associations as savings banks, attracted by the high rates of interest yielded on savings. For borrowers the common practice is to subscribe for a number of shares sufficient to cover their loan. Thus on a $2,000 loan a borrower would subscribe for ten shares at $200 each. His carrying charge would amount to $1 per month per share as dues and, when the rate of interest is figured at 6 per cent, $1 per month per share for interest. Under this plan the loan would normally be amortized in 16 or 17 years. Actually it may be amortized several years sooner since the borrower, paying 6 per cent on the original loan, is really paying much more than 6 per cent for the use of the funds. The association, being co-operative in nature, distributes these extra earnings among the shareholder-borrowers, thus enabling a more rapid reduction of the principal.

At the end of 1941 there were 7,207 building and loan associations in the United States. These associations numbered 6,978,057 members and showed assets of $6,053,345,616. The following table shows the expansion and decline of building and loan associations over a 22-year period.[3]

[1] Census of the United States, 1940 *Housing*, Fourth Series, Supplement A, p. 4.

[2] Bemis, vol. 2, chap. 7.

[3] *Monthly Labor Review*, vol. 41, p. 1513; vol. 43, p. 1433; vol. 46, p. 107; vol. 48, p. 336; vol. 52, p. 127; United States Savings and Loan League, *Annual Report*, 1940, 1941.

TABLE XXXVII.—NUMBER, MEMBERSHIP, AND ASSETS OF BUILDING AND LOAN ASSOCIATIONS, 1920–1941 *

Year	*Number of Associations*	*Membership*	*Total Assets*
1920	8,633	4,962,919	$2,519,914,971
1921	9,255	5,809,888	2,890,761,621
1922	10,009	6,864,144	3,342,530,953
1923	10,744	7,202,880	3,942,939,880
1924	11,844	8,554,352	4,765,937,197
1925	12,403	9,886,997	5,509,176,154
1926	12,626	10,665,705	6,334,103,807
1927	12,904	11,336,261	7,178,562,451
1928	12,666	11,995,905	8,016,034,327
1929	12,342	12,111,209	8,695,154,220
1930	11,777	12,350,928	8,828,611,925
1931	11,442	11,338,701	8,417,375,605
1932	10,997	10,114,792	7,750,491,084
1933	10,727	9,224,105	6,977,531,676
1934	10,920	8,370,210	6,450,424,392
1935	10,534	7,059,567	5,888,710,326
1936	10,256	6,125,971	5,741,935,430
1937	9,762	6,233,019	5,711,658,410
1938	8,951	6,829,167	5,629,564,869
1939	8,328	6,499,511	5,674,262,030
1940	7,738	6,758,354	5,794,529,850
1941	7,207	6,978,057	6,053,345,616

* See footnote 3 on page 469.

A common practice among insurance companies is to make loans up to a maximum of 50 per cent of the market value of a house and lot. Mortgages run from 10 to 15 years, being regularly liquidated by means of monthly, quarterly, or semiannual payments. In some cases the borrower is required to provide additional security in the form of a life insurance policy, purchased from the lending company, equal to the amount of the loan.

Lending practices of savings banks are much the same, except that they do not usually require amortization of the loan. By this procedure they avoid the necessity of reinvesting fairly large sums. As long as interest payments are made regularly on real estate whose value does not shrink, there is usually no particular reason why savings banks should require payment of the principal in installments.

The usual method of financing the purchase of a home is to secure the necessary loan from one of the above-mentioned lending agencies, giving as security for repayment a mortgage on the property. This means that the lender has a conditional title to the property and is given the right, in case of default in payment of interest or principal, to foreclose the mortgage and thus have the property sold to satisfy

his loan. Mortgages are classified as first, second, and third, although third mortgages are not common. The holder of a first mortgage has a prior claim, in case of foreclosure, over the holder of later mortgages. Among insurance companies and savings banks it is customary to make loans on first mortgages up to a maximum of 50 per cent of the prevailing market value. Building and loan associations, however, sometimes loan on first mortgage up to 60, 70, or even 80 per cent of the market value. In such cases their interest rates will probably be higher, ranging from 7 to 10 per cent, as compared with a range of from 5 to 7 per cent charged by insurance companies and savings banks.

Nominally interest rates on second mortgages are usually the same as on first mortgages. This is usually the case where the state law sets a maximum legal rate of contract interest. Actually there is wide disparity among interest rates on second mortgage loans. By use of fees, dues, premiums, commissions, service charges, and discounts, the actual rates of interest may be increased even to 20 per cent or more. The discount method is one of the most common. Under this plan a borrower of $3,000, if he is charged a discount of 20 per cent, would really get only $2,400 but is obliged to pay back $3,000, besides paying interest on that amount. This device, together with the others mentioned, is used to evade usury laws. A typical rate of actual interest on second-mortgage loans is 15 per cent. It must be noted, however, that since second mortgages are usually for smaller sums, the total financing cost might range from only about 8.5 to 11.25 per cent if the borrower pays 6 per cent on his first mortgage and 15 to 20 on his second. This assumes that the first mortgage covers not more than 50 per cent of the market value and that the second mortgage covers 20 to 30 per cent. The importance of financing cost is emphasized by realization that an increase or decrease of interest rates by 1 per cent will affect rental rates or carrying charges as much as would a 10 per cent increase or decrease in direct costs of construction.[1]

Should One Own or Rent a Home?

Cost of Home Ownership. A good deal of maudlin sentimentality has been written about the joys and virtues of home ownership. A typical view is that "One of the greatest thrills in life is to walk up to the front door of the place you live in, turn the key and enter, and be able to say: 'This place is mine!' There are thrills about the place, sunlit, airy rooms, maybe a porch that is cool and breezy in summer time, a kitchen that is a real kitchen, maybe a garden to dig in healthfully, and in which

[1] Bemis, vol. 2, chap. 10.

to raise crisp vegetables, fresh fruits, and beautiful flowers. Does not the thought make you say, 'I *can* and I *will* own my home'?"[1]

A common proverb is that rent money is spent money. "It can easily be calculated that people who can afford to pay rent, and that means everybody, can afford to own their own home. . . . In New York the average tenant pays enough rent in ten years to equal the value of a house. This means that every ten years he buys the house from the landlord, and makes the landlord a present of it."[2] Such statements seem to imply that rent is a cost separate and distinct from the carrying charges involved in purchasing a home. It should be realized that the chief difference between renting and owning is that the renter buys the services of a house from month to month while the owner buys the house outright in order to secure its services. What are the relative costs of these two methods? One answer is found in the average expenditures for owned and rented family homes as revealed in the survey of family expenditures for 1935–36. Table XXXVIII compares these expenditures for farm, rural-nonfarm, and urban families at several different income levels. The expenditures for farm families include the money expense of repairs, replacements, insurance, and the imputed rental value of the owned family dwelling. For nonfarm families, the expenditures for housing include the money expense for interest on mortgages, refinancing charges, taxes, special assessments, repairs, replacements, and insurance, as well as the net imputed rental value of the owned family homes. The figures in column three showing the ratio of expenditure of owning to renting families are computed by dividing the average figure in column 1 by the figure in column 2. It will be observed that the number of families owning their own homes is relatively small for urban residents in the two lower income levels. In every case but one the expenditures of owners exceed those of renters.

It will be recalled that among the 1,400 families of Philadelphia hosiery workers those who owned their homes were paying $47.60 a month for the use of their houses, while those who were renting paid $28.35 per month. In the 1940 census of housing it was found that the median rent of tenant-occupied homes was less than the median rental value of owner-occupied homes, in urban, rural-nonfarm, and rural-farm areas of each region of the country. For the nation as a whole the median rent of urban and rural-nonfarm homes was $21.41 for tenants and $27.45 for owners.[3] In a period of rising prices or in case of a housing

[1] Blodgett, Harvey A., *Making the Most of Your Income*, p. 103, by permission of The Macmillan Company, publishers, New York, 1933.

[2] Davis, Jerome, *Contemporary Social Movements*, p. 545, D. Appleton-Century Company, New York, 1930.

[3] Census of the United States, 1940, *Housing*, Series H-13, No. 11.

TABLE XXXVIII.—AVERAGE EXPENDITURES FOR OWNED AND RENTED FAMILY HOMES OF FARM, RURAL NONFARM, AND URBAN FAMILIES, AT SELECTED INCOME LEVELS, IN THE YEAR 1935–36[1]

Income Level and Type of Community	*Average Expenditure for Family Home of Families*		*Ratio of Expenditure of Owning to Renting Families (per cent)*	*Proportion of Single-Tenure Families*	
	Owning Throughout Year	Renting Throughout Year		Owning Throughout Year (per cent)	Renting Throughout Year (per cent)
$500–$1,000:					
Farm	$109	$ 59	184.7	42.4	57.6
Rural nonfarm	171	112	152.7	36.4	63.6
Urban	215	175	122.9	21.3	78.7
$1,500–$2,000:					
Farm	206	172	119.8	66.2	33.8
Rural nonfarm	252	199	126.6	48.4	51.6
Urban	343	304	112.8	35.1	64.9
$3,000–$4,000:					
Farm	329	237	138.8	76.2	23.8
Rural nonfarm	371	288	128.8	75.9	24.1
Urban	523	506	103.4	54.0	46.0
$5,000–$10,000:					
Farm	461	321	143.6	92.6	7.4
Rural nonfarm	488	351	139.0	82.5	17.5
Urban	887	927	95.7	63.8	36.2

shortage it is quite possible that these figures would be reversed. This means that in general money costs of home ownership may be less if houses are scarce or if prices are rising. This is because financing costs are usually arranged on a long-time basis and do not fluctuate with short-run price changes. On the other hand, it may be cheaper to rent if there is a large supply of houses available or if the general price level is falling. In short, " . . . rent bears little relation to the original cost. The renter may pay more or less than is required to cover the landlord's costs. The renter takes advantage of periods of decline in rents and the landlord takes advantage of rises."[2]

From an economic point of view rent may be explicit or implicit. Explicit rent is the amount paid out by a tenant to another person who owns the house. Implicit rent includes the amount paid by the owner under the usual phrase "carrying charges" for the dwelling. What do these include? In contrast with the renter whose monthly check absolves him from all further financial responsibilities, the owner is responsible

[1] National Resources Planning Board, *Family Expenditures in the United States*, p. 10, United States Government Printing Office, Washington, 1941.
[2] *Monthly Labor Review*, vol. 52, p. 917.

for taxes, interest and principal payments on borrowed funds, repairs, depreciation, insurance, and assessments. For a rented house, the landlord, upon receipt of his rental check, becomes responsible for meeting these various expenses. The amounts involved will vary of course not only from house to house but among localities. Obviously if it costs nearly 27 cents a cubic foot to build a house in Providence, R. I., compared with 18 cents in Columbia, S. C., the Providence owner will have larger carrying charges. Interest rates may vary, as well as taxes. Owners in undeveloped sections face also the possibility of meeting assessments for sewers, water lines, curbing, paving, and sidewalks. If the owner has paid cash for his house the interest which he might have received if he had invested his funds elsewhere constitutes an implicit cost of home ownership. This means that if he paid $8,000 for his home and could have received 5 per cent if he had invested his $8,000 in some other form of wealth his house is actually costing him $400 a year. That this is true may be shown in another way. Suppose he finances his house by means of a first mortgage up to 50 per cent of its value. On the $4,000 borrowed from a lending agency he pays 5 to 7 per cent interest and regards the $200 to $280 so spent as a cost of home ownership. Clearly it makes no difference whether he borrows the funds from someone else or from himself; in either case a cost is involved. In addition to these costs which are permanent, there are other costs which usually come as a surprise to the uninitiated buyer of a home. These include fees for title search and guarantee, transfer costs, recording costs, legal fees, stamp taxes, and other unexpected charges. On a house ranging from $7,000 to $9,000, depending on locality, these transfer costs, as they are known, may vary from $100 to $200. While this may not be large when regarded as spent over many years, it looms unusually large at the time of transfer, when it must be paid in addition to all other expenses.

In spite of differences in localities the most common workable formula is that which holds that the cost of home ownership is roughly 10 per cent of the capital value. That is, on the $8,000 house the cost of ownership would be approximately $800 a year. If the owner were to rent the house he would have to receive at least that much if he were to earn a fair return on his investment after paying operating costs. If anything, this estimate is low. Bemis uses the figures 12½ per cent if depreciation is calculated at 1 per cent. If allowance for depreciation is increased, as it probably should be, to 2 or 3 per cent, the cost of home ownership increases to 15 or 16 per cent.

Is It Cheaper to Own Than to Rent? The answer to this question has been suggested in the earlier part of this section. Properly regarded as an economic investment, the costs of buying the services of a house,

whether owned by the occupant or by another person, are essentially the same in the long run. On a strictly comparative basis there might be a margin in favor of ownership equal to the administrative costs for which the landlord must in the long run secure reimbursement. Why is it that popular belief holds that owning is cheaper than renting? The reason is no doubt found in the fact that probably very few owners consider interest on their own investment as a cost. That is a sum which need not be paid out to anyone else. If the capital invested in the house had been invested elsewhere so as to yield 5 or 6 per cent that return would be regarded as income; but if the owner denies himself that income in order to invest the sum in a house he usually fails to regard the lost income as a cost.

Another reason why owning is considered cheaper than renting is that very few private owners include a charge for depreciation. As a matter of fact, there are probably few home owners who keep any accounts. To them costs of ownership are simply those which have to be paid out to someone else. Like interest on one's own investment, depreciation is not such a cost.

This being the case, those persons who own their homes clear of mortgage have only such expenses to meet as taxes, repairs, insurance (and not all carry this protection), and assessments. These expenses may amount to no more than 4, 5, or 6 per cent of the capital value. The commonly regarded costs of owning an $8,000 home would therefore be from $320 to $480 a year. While this method of regarding home ownership may be comforting it is not financially sound.

For many American families the question whether it is cheaper to own or to rent is purely rhetorical. The naïve view that anyone who can afford to rent can afford to own simply does not stand the test of practicality. Of 29,400,300 families 80 per cent, or 23,520,240, had total incomes of less than $2,000 in 1935–36, the latest typical peacetime year for which reliable figures are available. No one with an income of less than that amount should, or probably could, try to own a home. A simple calculation will show the reason for this statement. If 20 per cent of the family income is budgeted for rent, and this is a high allowance, that would amount to less than $400 a year. Including all proper costs of ownership, $400 a year would purchase only a $3,300 house. Considerable evidence has been presented showing that typical low-cost houses range from $4,000 to $5,000. Houses with sunlit, airy rooms and a garden for raising vegetables and flowers, such as Mr. Blodgett describes, would cost two or three times that amount. It might be well at this point to re-read, earlier in the chapter (page 461), the description of a $6,000 house which did not include land and other important items such as

gas range, water heater, screens and window shades, lighting fixtures, or interior decoration. " . . . Recognition is gradually growing that home ownership is neither desired by, nor desirable for, a large proportion of our citizens. To provide for them rented homes which they can rightly regard as more than places of temporary abode between moving days is coming to be regarded as an important segment of the housing problem."[1]

There are, however, a great many families whose annual income is sufficient to warrant ownership of a home. In deciding this important question there are, as is true of so many economic decisions, a number of other factors to be considered in addition to relative cost.

Other Factors to Consider. There are times and places where or when the only way to secure desirable living quarters is to buy or build a house. In an old community, for example, while there may be many rentable houses none of them may be completely equipped with modern conveniences. Or it may be that when a family is looking for a house, rents are temporarily very high so that it appears cheaper to buy or build. In such cases prospective owners would do well, however, to take the long-run point of view. If rentals are high it is more than likely that building costs also will be high. It must be remembered also that rentals vary over long periods of time. Excessive rentals in one period may be offset by lower rentals a few years later. In cases where home ownership is decided upon, purchase or construction should be undertaken in periods of depression rather than in periods of prosperity. There is a contagion inherent in building booms which is likely to cause individual buyers or builders to assume financial obligations which may be difficult to meet at a later time.

Allusion has been made to the relative desirability of houses for rent compared with those which can be bought or built. Even though it may be cheaper to rent than to own, a family possessed of sufficient financial resources may prefer to incur the added expenses of ownership in order to secure more desirable living quarters.

Probable permanence of employment is an extremely important consideration. If the family head is full or part owner of a business whose permanence is fairly certain, there is much less risk involved in home ownership. This is true also for a professional man whose location is quite certainly permanent. For that large body of persons whose tenure of employment is dependent upon factors quite largely beyond their control, home ownership carries rather serious hazards. Considerable

[1] "Home Financing" in the Duke University Law School's journal *Law and Contemporary Problems*, vol. 5, Autumn, 1938, p. 480; see also an article by Louis, Charles F., "Large-Scale Rental Development as an Alternative to Home Ownership," *Law and Contemporary Problems*, vol. 5, Winter 1938, pp. 602–607.

indeed are the losses of families who, desiring to change their location, are compelled to dispose of their homes. This necessitates forced sales at sacrifice prices, or if the property is retained the owner involuntarily becomes a landlord. Under the necessity of renting living quarters in his new location, the owner finds his budget for shelter suddenly doubled during times when his former home is unoccupied.

Hazards of home ownership are particularly great for that group known as wage earners. Ownership operates in favor of conservatism and immobility, both of which are advantageous for employers. Classical wage theory holds that wages for workers in the same group will tend to seek the same level in different localities as a result of the movement of workers from low-wage to high-wage centers. While there are many influences such as family ties and friendships which hold even non-property-owning workers in localities where wages are lower than elsewhere, home ownership operates very definitely thus to reduce mobility of labor. Fear of losing their equity in a home may cause workers to remain with an employer whose wage scale is lower than might be obtained for similar work in other communities. Property ownership tends to identify the interests of employer and employees by implanting what is known as the capitalist viewpoint in the minds of employees. This fosters a conservatism which has often proved a formidable obstacle to labor organization. It is not without reason that open-shop employers are usually strong believers in and propagandists for the virtues of home ownership among their employees. Increasing hazard of unemployment resulting not only from business depressions but from unforeseen technological changes should cause workers to weigh carefully the assumed advantages of ownership against its possible losses. An authoritative student of labor problems concludes that "It is in fact very doubtful whether, in view of the present uncertainties of industry, it is wise for most manual workers to attempt to own their own homes."[1] It may be added, in passing, that the discouraging effect of unemployment on home ownership is used effectively as an argument in favor of stabilizing workers' incomes by means of unemployment insurance.

A fourth factor which prospective owners must consider is the expense of living in the locality where they wish to settle as owners, as compared with the expense of living elsewhere as renters. One of these items is transportation. Formerly confined largely to budgets of city dwellers, the automobile has increased the tendency of persons to live at some distance from their work. Outlay for trolley, bus, or automobile may vary from a minimum of $2.50 a month to $15 or $20 or even more.

[1] Douglas, Paul H., and Director, Aaron, *The Problem of Unemployment*, p. 147. By permission of The Macmillan Company, publishers, New York, 1931.

The scale of living in the neighborhood under consideration should be ascertained. Many a family has incurred financial difficulties by moving into a section where their neighbors, as a result of either larger incomes or greater improvidence, maintain a scale of living beyond that which the newcomers can afford. Efforts to keep up with the neighbors are almost as certain to bring unhappiness as failure to make the attempt. A survey of 631 families who had just purchased or rented new homes indicated that they spent an average of $473 per family for furniture and furnishings upon moving into their new location.[1] Cost of houses in the prospective location should be compared with costs in alternative areas. Site values may exceed those in other locations by an amount greater than is warranted. When prices for houses in one area are too high, it may be possible to secure equally desirable homes in another vicinity.

A fifth factor to be considered is the possible gain of living near one's business. Although actual cost of home ownership there may be greater than rentals or home-owning costs elsewhere, the excess may be offset by increasing returns resulting from living in close proximity to one's place of business. This consideration is probably confined largely to smaller communities, where personal relationships are more significant. To be able to say that one is a tax-paying property owner often promotes good will. This is demonstrated by the tendency of chain-store managers in small towns to court community favor by assuming the role and responsibilities of tax-paying citizens.

An additional factor for prospective property owners to consider is possible appreciation or depreciation in capital value. There is frequently a possibility that property values may rise, enabling owners to realize a speculative profit. On the other hand, there is always the possibility that property values will decline. Such depreciation may result from a number of causes. Without attempting to enumerate all of them it may be noted that among the more common causes are business depressions, overexpansion, and growth of blighted areas.

Now that the income tax base has been broadened so as to include a much larger number of income receivers, another factor to be considered in choosing between home ownership and the rental of a house is the favorable treatment accorded the home owner by the Federal personal income tax law. Since imputed rent is not considered income for tax purposes the home owner is favored as compared with the renter. Under current income tax rates, this fact may swing the balance in favor of home ownership.

Advantages Claimed for Home Ownership. Perhaps this extended discussion of the question whether one should own or rent a home may be

[1] *Printers' Ink*, June 18, 1943.

recapitulated best by presenting for purposes of summary a contrast of the advantages commonly claimed for each method of procedure. In favor of home ownership it is contended that after a period of several years the person who has been purchasing his home is the proud possessor of a valuable investment rather than the mere holder of a bundle of receipts. Desire for and achievement of home ownership is alleged to encourage thrift. Ownership of a home assures a permanent residence. This is regarded as particularly desirable in the case of a widow with a small income. A home owner has fixed annual costs in contrast with fluctuating, uncertain rents. The family which owns its home enjoys a higher credit standing, and finally, it is claimed that home ownership develops good citizens who are interested in good government.

Objective critics of these claims point out that while the homeowner may possess an investment instead of a bundle of receipts there is always the possibility that he may own a liability instead of an asset. The phrase is held to be misleading, moreover, because it implies that less has been received for rental payments than for purchase payments. The renter has actual day-to-day use of the house, which is exactly what he pays for and which is all the homeowner receives. It is true that ownership encourages thrift but it is also true that an unfortunate investment may discourage thrift. It is true that the homeowner is assured of fixed annual costs but that is not necessarily nor always an advantage. If those costs have been incurred during a period of high prices they persist in a period of low prices, whereas the renter secures any advantage of declining prices. Admitting that home ownership develops good citizens' interest in good government, it is contended that there is a strong probability that it may also develop persons whose primary interest is in maintaining the *status quo*. From the social point of view this may retard progress. There seem to be no adequate answers to the claim that ownership assures a permanent residence and raises the credit rating of the owner.

Advantages Claimed for Renting. It is claimed first of all that in the long run renting is cheaper than owning. If the cost of ownership is 12.5 per cent, as Bemis contends, it would appear that this claim has some statistical basis in fact. The second contention is that if the excess outlay required for ownership were invested wisely in some other form of wealth it would yield a better financial return.

Since the renter has no capital investment in real estate he does not face the hazard of shrinkage in capital value. To him slumps in real-estate prices mean gains rather than losses. The renter has no fear of the spread of blighted areas, nor is he concerned with increases in property taxes. If he loses his job he does not stand to lose whatever equity he might have had in a home. If opportunity develops for him to increase

his income by moving elsewhere he is foot-loose and free to make a change. In some apartment houses the problem of living is simplified, since one check for rent pays not only for shelter but also for heat, light, gas, and janitor and maid service. Such an apartment-house dweller is not worried over the price of coal, rates for electricity or gas, or burdened by the problem of securing household help.

Many of the answers to these claims have been suggested. To the contention that renting is cheaper than owning it is argued that home ownership is something more than a cold-blooded business. Perhaps the owner should include interest on his own investment and depreciation as costs of ownership, but after all these need not be met in the form of monthly payments. If they are disregarded, perhaps ownership is cheaper than renting. Admitting for the sake of argument that there is an excess outlay in ownership which might be invested in other ways, two questions may be raised. Will the renter actually save the surplus or will he fritter it away? If he does save it, is there not equal danger that capital values in other types of investment will shrink? There are also two replies to the contention that renters need not be concerned over increased property taxes. According to the theory of prices, rentals on real estate must in the long run be at least high enough to yield a gross return which will cover the owner's expenses and yield a fair return on his investment. Otherwise owners will fail to maintain existing property, while investors will fail to build new houses. Thus in the long run the tenant is actually paying taxes whether he realizes it or not. Laboring under the illusion that taxes are not their concern, renters are inclined to take their duties as citizens too lightly and to vote for increased governmental expenditures without regard to the probable source of revenue.

There can be no doubt that renters are free to move, but to some people this is a fault rather than a virtue. It is complained that renters, especially urban apartment-house renters, are essentially nomadic. This is particularly true of those who rent furnished living quarters. For millions of people the modern apartment is nothing more than a "homette" which provides shelter and a place to store a bit of extra clothing and perhaps a few household goods. Certainly such living does not develop virtues commonly attributed to home ownership.

The question of ownership versus renting is indeed a moot one. For a long time arguments for and against ownership have been given and the controversy will continue. The various arguments have different appeals to different people. Arguments which were valid in one generation are not valid in another. The most that can be said safely is that on the basis of those here presented each individual family will have to reach its own decision. It is too much to hope that all future owners will

consider the question as carefully as this discussion indicates they should; but for those who do weigh all factors involved and then proceed to purchase or build a home there is much greater likelihood that the decision will be that of economic men and women and will lead to satisfaction and happiness rather than disillusion and disappointment.

Summary

Next to food, shelter is the greatest need of consumers. Provision of living quarters requires 15 to 18 per cent of family income, yet that expenditure fails to yield desirable houses. Construction costs for dwellings are high, ranging from 1.5 to 3 times a year's income. This means that many people cannot afford to own their homes.

While very great improvements have been made in housing accessories and appliances, very little progress has been made in dwelling construction. There are many reasons why construction costs are high: —the localized nature of the business, inefficient organization, excess capacity, the seasonal factor, financing costs, legal restrictions, and taxes.

Installment buying of homes has long been common. Credit is supplied chiefly by building and loan associations, insurance companies, and savings banks. Financing costs range from 5 to 10 per cent on first mortgages and from 15 to 20 per cent on second mortgages. Total financing cost may vary from about 8 to 12 per cent.

Much confusion in thinking centers around the question of home ownership. Properly regarded, long-run costs of ownership will be nearly identical with rentals. In the short run, variations will occur depending on such factors as depression, housing shortage, and changing price levels.

Whether a family should own or rent is a subjective problem. In addition to comparative costs there are other factors to consider, such as availability and desirability of houses, permanence of employment, possible gain from living near one's place of occupation, and possible rise or fall in property values. Advantages claimed for owning and renting will hold different appeals for different people. A decision based on consideration of all factors involved will be more likely to result in permanent satisfaction.

QUESTIONS FOR DISCUSSION

1. Should everyone own a home?
2. Does your family own its home free of debt? If so, how much implicit rent do you estimate is being paid? How will this item appear in the family budget?
3. How should a modern home be constructed? What features should it possess? Of how many such homes do you know?

4. Would it be wise to remodel an old house that you like?
5. If there is such a shortage of desirable dwellings in the United States why is there not a building boom?
6. Can you offer any explanation for the failure of the building construction industry to develop the mass production methods used so successfully by the automobile industry?
7. How do installment credit costs in the building construction industry compare with those in the sale of automobiles? Home furnishings?
8. Considering only the economic aspects of the question, would you prefer to own or to rent your home?

PROBLEMS AND PROJECTS

1. Make an estimate of the total value of housing in your community, separating land values from building values. What are the housing facilities, in terms of rooms, per family? In your report include a brief summary of architectural styles.

2. (To be shared by several members of the class.) Take a sample of 10 or 20 homes in your vicinity, occupied by persons in about the same economic class, and secure the following information:

a. How many own their homes?

- i. What was the purchase price?
- ii. How were they financed?
- iii. How many are free of encumbrance?
- iv. If mortgaged, to what extent?
- v. What is the average or median family income?
- vi. What do you estimate is the annual cost of owning these homes? What does this cost include?

b. How many rent their homes?

- i. What is the average or median rental?
- ii. What is the average or median family income?
- iii. What is the proportion of rent to income?

3. Examine the real estate records in your county courthouse (or elsewhere) to ascertain what proportion of residential properties is mortgaged and by what type of credit agency the mortgages are held.

4. If you have a local building and loan association write a report on its history and operation, emphasizing the volume of mortgage loans and costs to borrowers.

5. (*a*) Assume that you are going to build a house. Choose your location, secure your plans, get estimates, and make forms for the necessary contracts. Or, (*b*) assume that you are going to buy a house. Plan all the necessary legal steps, and your financing. In either case make a final calculation of your carrying charges.

6. Write to four or five producers of pre-fabricated houses for information, plans, and financial arrangements. If you find a suitable house, choose a location for it, then plan completely your financial arrangements, and calculate your annual or monthly cost.

23

Buying Investments

The Consumer Seeks to Save

The Meaning of Investment. Strictly speaking, investment is a form of spending. In one sense, all wise spending is a process of investing. The purchase of good food which will build strong bodies yields rich returns in good health. The purchase of good clothing yields protection and satisfaction. The purchase of a home is an investment in shelter. The purchase of insurance is an investment in protection. The purchase of educational training, of travel facilities, and of many other such intangibles represents investment in the broad sense.

But the term investment as used in this chapter means the spending of money for the purchase of property, especially for its income-yielding power. Although popular thought distinguishes between spending as the paying out of income for consumers' goods, and saving as the deposit of money in an institution or as the purchase of securities, it is obvious that in either case the one parting with purchasing power is spending. The only difference is in the purpose for which the spending is done. As the terms are used in this discussion, the distinguishing feature is that in buying investments one is purchasing other forms of wealth, or claims to wealth, which are expected to yield a subsequent income in cash.

When and How Much Should One Save? Writers on investments and family finance are quite generally agreed that a family head should make little or no effort to save for the purpose of future income until he has provided adequate insurance protection, a home free of debt, and a savings account of from one to three thousand dollars to meet emergencies. Obviously such a program means that millions of families will have no surplus for investing. Let it be emphasized that this does not mean that such families are not saving. In the economic sense, saving is the postponement of consumption of a certain portion of one's income. A family head who has provided adequate insurance protection will have arranged for the continuance of an income which will enable his survivors to maintain their accustomed plane of living in the event of his premature death. The previous discussion of insurance shows clearly that such a program involves not only spending for protection but a considerable amount of saving in the form of accumulated reserves.

Professors Huebner and McCahan have made out a strong case for *Life Insurance As Investment*, emphasizing the record of security during severe depression. Other advantages include liquidity and favorable tax treatment. Annuities represent pure saving and as such are better suited as investments for small savers, having all the investment advantages of life insurance.

Likewise, if a family head has provided a home he has, according to usual standards, saved from two to two and a half times his annual income. A man with a $2,000 yearly income would normally provide a family home worth $4,000 to $5,000. If this were clear of debt it would, of course, represent a saving of that amount, but not an investment as defined in this chapter. Likewise, a savings account of from $1,000 to $3,000 is primarily a saving rather than an investment, since its purpose is to be held as a reserve to meet emergencies rather than to yield income. Such interest as may be received on a savings-bank account would be incidental rather than the chief motivation for saving.

Such a program of saving means that millions of families cannot possibly have any surplus for investment purposes. As an illustration let us assume that A, a married man with three children, has a yearly income of $2,500. According to the standard of adequate insurance set up by insurance experts, he should carry enough life insurance to yield approximately $1,250 annual income. This would cost at least $400 a year in premiums, varying with his age. Following the general rule, his home should cost not over two and a half times his annual income, so that he should have a family dwelling costing from $5,000 to not over $6,250. Finally, he should have from $1,000 to $3,000 in the savings bank. Suggestions as to how much a family should save range from 5 to 20 per cent of income. The latter figure is the maximum suggested. If Mr. A were to save up to the maximum, his family would have $2,000 annually on which to live and he would have $500 to put into insurance, a home, and a savings account. If he were to carry adequate insurance protection that would require at least $400, leaving only $100 for the savings account and nothing for the purchase of a home. Of course few if any men with such an income would carry more than $10,000 or $15,000 worth of insurance. Some might carry less insurance and put the balance of their savings into a home or a savings account. In any event it seems clear that a family with a $2,500 income would have no funds for investment. This means that according to 1935–1936 figures over 25,500,000 families, or 87 per cent of the total, having incomes of $2,500 or less, were unable to make any investments.

There are, however, over 3,000,000 families with annual incomes in excess of $2,500, and several millions of unmarried consumers, who

do have savings to invest. Without doubt, also, several other millions of family heads, who carry less than the prescribed amount of insurance, or do not own a home, or do not have from $1,000 to $3,000 in a savings account, choose to buy investments in the form of bonds or stocks. What guides can they follow when they enter the market place? Although consumers have been shown to be woefully uninformed buyers of consumers' goods and services, some of these people who have funds to invest are, if anything, even less informed. The naïve notions held by amateur investors, and their positive disregard of all ordinary rules of precaution, are amazing. As a result fraud is prevalent, and waste in the form of losses runs into millions of dollars annually. A Congressional investigation in 1930 revealed that American investors had lost $25,000,000,000 in the purchase of worthless securities in the preceding decade. Just as buyers are the victims of bargain lures in purchasing consumers' goods, so are amateur investors victims of get-rich-quick lures in purchasing investments. When the consumer is swindled in the purchase of a commodity it is a misfortune, but usually the amount involved is not large. When an investor is swindled, although the amount may not be large, it probably represents all of his savings accumulated as a result of considerable sacrifice. It is all the more important that small investors follow and profit by the experience of others.

How Should One Invest?

Two General Types of Investment. There are two general types of investment, those establishing a creditor status and those establishing a proprietor status. The former type of investment is exemplified by savings deposits, the purchase of shares in building and loan associations, and the purchase of bonds or mortgages. In each of these cases the investor is lending his funds with the hope and varying degrees of assurance that he will receive interest for their use and return of the principal intact when the loan is due. Several risks are involved in such a transaction. The greatest of these is the possibility that the borrower may be unable or unwilling to return the principal amount. As a safeguard, lending agreements usually call for some form of security in the form of hypothecated wealth.

If an investor with several thousands of dollars to invest decides to purchase a gasoline filling station he would find quickly that as the proprietor he had assumed a great many duties and obligations. He would have to spend considerable time managing his business, arranging for deliveries of supplies, meeting the bills for them, paying taxes, keeping his property in repair, hiring necessary additional help, purchasing insurance to cover risks of customers, employees, and property, and

arranging perhaps for credit facilities at his bank. In return for his services he would receive whatever surplus remained after meeting all other obligations. In this illustration the risks and responsibilities incurred by the investor are unmistakable. What is not so clear is that if this investor, instead of putting his savings into a gasoline filling station, should purchase several shares of stock in an oil refining and distributing company, the difference in risk and responsibility incurred would be one of degree rather than one of kind. As a minority stockholder he might take no active interest in the management of the corporation of which he was a part owner. Nevertheless someone to whom he and other stockholders have delegated authority would have to assume the responsibilities of management. If the business should fail, the stockholders would lose not only their anticipated income, but also the savings which they had invested.

Investors Fall into Two General Groups. There are two general groups of investors, those whose investments are small and made indirectly, and those whose investments are large and are made directly. The small indirect investors are the ones who put their savings into savings banks, building and loan associations, or similar savings institutions. They take a smaller return on their savings, for the privilege of having more qualified specialists select their investments for them. If one has only a small amount to invest, such as $1,000 or less, it is usually wiser to invest it in this way. Generally speaking, the smaller the investment, the greater the importance of security. Second in importance is the ease with which the investment can be converted into cash, while the item of third importance is that of income. While it is true that savings banks pay investors only a small rate of interest on their savings it is true also that under the Federal Deposit Insurance Corporation a high degree of security is assured such investors. Probably the best that a small investor can do in the way of income with comparative security would be $3\frac{1}{2}$ to 4 per cent. By taking the smaller rate from a savings bank he secures a number of services, such as the benefit of more experienced investing judgment and a wide diversification, which should mean greater security. Moreover, bank officials relieve him of the responsibility of investigating and comparing innumerable issues of securities and assume for him responsibility of safe keeping, once the securities have been purchased.

In the case of the second group of investors, whose investments are large and direct, it is presumed that they have several thousand dollars yearly to invest and are able and willing to study the market in general and various security offerings in particular. On the basis of their own analysis or that of a paid counselor they decide what changes to make in their investment portfolio. For such investors this brief analysis is not written.

INVESTMENT OR SPECULATION?

What Is the Difference? Investment has been defined as the spending of money for the purchase of property for income, in which security, liquidity, and income are matters of greatest concern in the order in which they are named. There is an inescapable conflict between the desire for security and the desire for income. Efforts to maximize one invariably result in minimizing the other. An investor may have a high degree of security if he will be satisfied with a comparatively small yield. Another investor may be receiving a comparatively large income, but with greatly reduced security of his principal. And one step further in this direction we come to the fundamental difference between investment and speculation. *Investment seeks to conserve the principal, while speculation seeks to increase it at the risk of losing it.* A speculator is not so much interested in the rate of interest or dividends paid on a security, as in the probable market price of the security at a later date. He buys a security, or other property, even land, in hopes of being able to sell it at a higher price soon. Speculation is often little more than gambling. A general rule which small investors might do well to follow is that which holds that securities yielding more than twice the return available on United States Treasury bonds are too risky. In fact some writers place the ratio as low as one and one-half times. This would mean that investors would be interested only in securities yielding 4½ to 6 per cent, depending on which ratio they chose to follow.

It is well for small investors to remember that investment is a science, while speculation is an art. Actual calculations based on customers' accounts with brokers of the New York Stock Exchange show that the chances of success in speculation are only one in five. If the stock is listed on an inferior exchange the chances of a successful speculation are less than 1 per cent. Any small investor who thinks he can beat the game should invest three dollars in John T. Flynn's *Security Speculation* or *False Security* by Bernard J. Reis before he invests three hundred or three thousand dollars in some highly speculative stock. Careful reading of one of these books should convince the intelligent small investor that the art of speculation is too expensive a pastime for him to undertake. In this uncertain world it is scarcely wise for those with savings deliberately to take unnecessary risk.

THE ORDER OF INVESTMENT

Different Kinds of Bonds. A bond is a promise to pay a certain sum of money on or before a specified date, with interest at an agreed rate. There are literally innumerable kinds of bonds, which may be distinguished in a number of different ways. One of these is by the type of

debtor. The two general types are governmental and industrial, the latter including public utility corporations subject to public regulation. A second basis for distinction is that of security. Many bonds have no specific security for their repayment. This is true of all governmental bonds and of a great many industrial bonds. In the latter case they are usually referred to as debentures. Most industrial bonds are secured by some pledge of property which is forfeited in case of default, becoming the property of the bondholders to be disposed of by them, and the proceeds to be used to pay off the bonds. A special type of security is the mortgage bond, which in turn has many variations. Usually a first mortgage bond is considered excellent security, while subsequent property liens are of doubtful value in case of forced liquidation.

A third basis for distinguishing bonds is their provision for repayment. While perpetual or extremely long-time bonds are fairly common in Europe, they have not proved popular in the United States. Sinking-fund bonds provide for their payment out of earnings of specified sums paid into a sinking fund for the ultimate retirement of the bonded debt. In the case of such enterprises as mining, where the vein ultimately will be worked out, this type of provision for repayment offers greater assurance to the investor. Serial bonds are retired in installments at definite periods indicated in the bonds, while callable bonds must be turned in by the investor when called for at previously agreed-upon terms which usually involve a premium.

A fourth distinguishing basis is the provision for interest payments. Most bonds provide for interest at some fixed per cent, default on which makes the principal fall due and enables the bondholders to foreclose. Income bonds contain no provision for fixed interest. These are usually issued by very weak, reorganized industrial companies whose securities are accepted by holders under compulsion.

A final basis for distinguishing among types of bonds is the special privileges which some of them carry. For example, many carry the privilege of tax exemption, while industrials may contain provision for conversion into other bonds or stocks, may include stock subscription warrants, and in rare cases may provide voting rights or participation in earnings. Generally speaking, such special privileges are designed as lures to unwary investors, the purpose being to attract them to bonds which are fundamentally weak.

United States Government Bonds. It is quite natural that national government bonds should be the standard by which all others are judged. Such bonds are issued by a sovereign power, their security resting not on a pledge of physical property nor on earning power, but rather on the power to tax. The value of such bonds depends entirely

upon investors' confidence in the ability and willingness of their government to repay its debt. In a democratic government such confidence is ultimately a reflection of the citizens' confidence in themselves as a group, for they constitute and compose the final authority.

The fact that Federal government bonds are a standard by which all others are judged may be established by another line of reasoning. The nation as a unit is far stronger than any individual business enterprise or any one of the separate states, counties, or municipalities. It is a matter of record that investors lose confidence, and justifiably so, in the bonds of some civil and industrial units while still retaining full confidence in the bonds of their Federal government.

Recalling the consensus of agreement among writers on investment, it may be concluded that a small investor, who has provided according to his own judgment adequate insurance, a home, and a savings account and has a surplus to invest, can secure greatest security and liquidity by purchasing United States government bonds. Whereas bonds usually are issued in large denominations of $1,000 or multiples thereof, the United States government has made it possible for small investors to purchase what have come to be known popularly as baby bonds, in smaller and more convenient denominations. The traditional way of arranging for the collection of interest on bonds has been that of attaching coupons which are negotiable on specified dates for the amount of interest due. The smaller bonds which are now held in such large volume by small investors, provide for the payment of interest on an accrual basis. The investor pays $18.75 for the bond which at the specified rate of interest will yield $25 at the end of ten years. On this basis, Series E bonds yield 2.9 per cent if held until maturity. Series E bonds are redeemable at any time, except within the first sixty days after they are purchased, on the following basis:

TABLE XXXIX.—REDEMPTION VALUES OF SERIES E BONDS, ISSUE PRICE $18.75

First ½ year	$18.75	5 to 5½ years	$20.50
½ to 1 year	18.75	5½ to 6 years	20.75
1 to 1½ years	18.87	6 to 6½ years	21.00
1½ to 2 years	19.00	6½ to 7 years	21.50
2 to 2½ years	19.12	7 to 7½ years	22.00
2½ to 3 years	19.25	7½ to 8 years	22.50
3 to 3½ years	19.50	8 to 8½ years	23.00
3½ to 4 years	19.75	8½ to 9 years	23.50
4 to 4½ years	20.00	9 to 9½ years	24.00
4½ to 5 years	20.25	9½ to 10 years	24.50

State Bonds. While there is only one national government, there are forty-eight sovereign states with full authority to issue bonds based on

public credit. That investors have varying degrees of confidence in the ability and willingness of the several states to repay their obligations is a matter of record. While the bonds of some states may sell at a premium those of others can be disposed of only at a discount. The disparity is not so great now as it has been at times in the past. State governments have shown themselves more susceptible to surges of public opinion. In some cases the result has been a too rapid or too large debt accumulation whose repayment appeared to present an insurmountable obstacle. Historical records show that several states have repudiated their bonds. Although this does not mean that repudiation will ever occur again, it does explain why investors have good reason to be more skeptical in their purchase of state bonds than in their purchase of Federal government bonds, none of which have been repudiated or in default on interest payments. In comparing security it is important to remember that a state cannot be sued even by the holder of a defaulted or repudiated bond. More than a half century has passed since the last repudiation of a bond issued by a state, but as recently as 1933 three states were in arrears on interest payments on their debts.

Although there was a strong tendency for state debts to pile up after World War I, there has been a noticeable recent trend toward decisive steps for the limitation and liquidation of state indebtedness. Like the Federal government, each state has sovereign powers of taxation, and as a democracy its government is in the hands of its citizens. While this may lend assurance to investors within the state, it may not carry assurance to investors in other states.

County and Municipal Bonds. There are in the United States more than 3,000 counties, and more than 2,800 cities each having a population of over 2,500. This fact suggests that there is considerable variation among county and municipal bonds. Historical records show that repudiation has occurred and default is not uncommon. There is no standard by which an investor can judge the comparative worth of two county or municipal bonds. In their sale the rule of *caveat emptor* still prevails. An amateur investor, entering the market for the first time, might find an excellent county or municipal bond, but he would be just as likely, perhaps even more likely, to find himself the holder of a bond issued by an unknown local government whose debt is disproportionately large, whose government is corrupt, and whose tax system is bad. Such information should be obtained before, not after, purchase. This means that county and municipal bonds should be purchased only by wealthy individuals or institutions such as savings banks or life insurance companies with large amounts to invest. Such individuals or groups have the facilities for investigating bond issues before purchase.

It may very well be that a bond is a perfectly safe investment, but that the price at which it is offered is too high. If local government bonds are to be purchased by small investors such action should be undertaken only on the advice of a competent banker who, it may be presumed, is able to make an adequate investigation himself or who has received reliable information from some other source such as perhaps his correspondent bank in the county or city issuing the bonds.

Utility Bonds. Certain types of business enterprise, such as those supplying transportation, or electric, gas, or telephone services, have long been recognized as so invested with public interest that they are properly subjected to varying degrees of public regulation. Except for interstate transportation companies, most utilities are subject to state control. In some cases this control has proved efficient, while in other cases situations have developed where the utilities control the regulating commissions and in some cases almost control the state government. As a result of these conditions such institutions as insurance companies and mutual savings banks were very cautious and limited purchasers of utility securities before 1935. This does not mean that they are not still sufficiently cautious, but it does mean that investment in utility bonds should be completely avoided by the average small investor. It must be remembered that we are now discussing the bonds of private corporate enterprises whose ability to repay is dependent on their earning power. Analysis of that earning power is a task which requires the services of experts. To choose the best securities issued by American railroads, for example, would require a study of the records of 170 Class 1 railroad corporations.

Senate investigations revealing fraudulent practices in holding-company finance confirm the conclusion that small investors should be extremely cautious in purchasing securities offered by holding companies. If they insist upon investing their savings in utility securities they should do so only upon the advice of a competent banker and should consider securities only of those large operating companies serving well-known urban areas.

Investment Trusts. In principle the investment trust would seem to be the ideal solution of the small investor's problem. This is a device whereby a group of presumed experts in analyzing security issues pool the funds of many small investors, using the proceeds to purchase a diversified selection of sound securities. In theory, if the holding of one issue of bonds or stocks falls in value that loss will be compensated by the possible rise in value of other stocks or bonds in the investment trust portfolio. Likewise, the lower income of some securities will be offset by the higher income of others, while the greater insecurity of the latter

will be offset by the relative security of the former. This will operate to give the small investor the ideal combination of security, large income, and relative liquidity.

The shortcomings of the investment trust plan are those of practice rather than principle. Its record in the United States is due not to any inherent defect in the plan, but to the fact that too many unscrupulous promoters organize investment trusts not as a means of serving small investors but rather as a means of enriching themselves. This is achieved all too often at the expense of those who supply the funds. In practice the investment trust has offered diversification and convenient denomination, but there has been too much speculation and outright manipulation.

The following facts brought to light in a hearing before the Securities and Exchange Commission illustrate what has happened on a wide scale. In 1927 two men with $10,000 organized an investment trust in Boston. In nine years the original capital had been run up to $82,000,000, with 2,625,000 shares of stock outstanding. From 1927 to 1935 the net profits totaled $1,900,000. During that eight-year period the management costs totaled $1,200,000, while selling costs amounted to $5,700,000. In the words of one of the two founders of the enterprise, "It costs money to sell securities."

The experience of thousands of small investors justifies the conclusion that those with limited savings to invest should avoid the lure of the investment trust, unless it is a type which deals exclusively in bonds and mortgages.

To all intents and purposes modern insurance companies function like investment trusts. All the advantages claimed for investment trusts are inherent in the insurance company, with the added advantages of conservatism and public regulation. As an investment, life insurance companies present a record of an average return of 5.22 per cent over the twenty years from 1912 to 1931, with a 99.9 per cent safety record during the depression years 1930 to 1932.[1] The record from 1930 through 1940 shows a declining rate of net interest, however, and there is no way of knowing how much more the rate may decline.[2] If life insurance companies are to be used as investment institutions the investor should separate his insurance and his savings contracts so far as possible. This can be done by using term or whole-life contracts for protection and single premium or deferred annuity contracts for investment.

Mortgages. Legally a mortgage is a conditional conveyance of property as security for the payment of a debt, which becomes void upon payment. There are literally dozens of kinds of mortgages. Viewed

[1] HUEBNER, S. S., and MCCAHAN, David, *Life Insurance as Investment*, D. Appleton-Century Company, New York, 1933.

[2] See Table XXXIII, page 447.

historically, the real-estate mortgage is probably the oldest and most common. This includes mortgages on farms, with or without farm buildings, and on city lots, with or without buildings thereon. Chattel mortgages are those in which the property conditionally conveyed is personalty. Formerly this included such items of movable wealth as livestock, farm machinery, and certain types of household goods. Today the range has been greatly expanded as a result of the development of installment sales, most of which are secured by chattel mortgages on the property sold.

There may be more than one mortgage on a piece of property. Second mortgages are fairly common, while third mortgages are offered less frequently. Probably an extreme case is that of the Erie Railroad, which has had as many as seven different kinds of mortgages on its property.[1] In case of default, foreclosure proceedings may lead to the sale of the property by order of a court. After payment of the first mortgage in full any remainder is distributed to subsequent mortgage holders according to their priority. Thus in case of default, the holder of a third mortgage would receive no pay unless the holders of both the first and the second mortgages were first paid in full.

For investment purposes the only type of mortgage to be considered is that which gives a first and prior lien on real estate in good condition and well located. The amount of the loan secured by the mortgage should not exceed 60 per cent of the market value of the property. A mortgage purchased under such conditions may prove to be a very good investment. It is possible that a small investor may deal with a well-known local citizen of known integrity and if he secures a personal bond in addition to the mortgage he will have double security. Rates of interest on first mortgages have long been 6 per cent or better. During the depressed 1930's there was a tendency for first mortgage rates to settle around 5 per cent. This represents a fairly large return on a reasonably safe investment.

From the point of view of the small investor there are two serious defects in first mortgages. One is the difficulty of finding an individual mortgage for the exact amount which one has to invest. Mortgage denominations vary according to the needs of the individual borrowers. A prospective investor having $1,100 to invest may find it impossible to locate a prospective borrower who needs exactly that amount and who at the same time can offer acceptable security. A second and very serious defect in mortgages as investments is their lack of liquidity. Unlike listed bonds and stocks, mortgages have no continuous market wherein the

[1] Sakolski, A. M., *Principles of Investment*, p. 77, The Ronald Press Company, New York, 1925.

investor may liquidate his holdings in case of necessity. If the investor purchases a first mortgage for $1,100 to run ten years he may be quite unable to recover his principal before maturity, no matter how urgent his need may be. For this reason alone purchase of first mortgages is often restricted to investors who have enough savings so that they will not be embarrassed by inability to liquidate that particular portion of their investments.

The foregoing discussion implies what must now be stated positively. Direct ownership of real estate is not a good investment for a small saver. In addition to lack of liquidity is the disadvantage that ownership involves a proprietary status which carries with it responsibility for managing the property. Management requires maintenance, payment of taxes and insurance premiums, renting and collection of rentals. For small investors too much time is required and the margin is too small.

One circumstance justifying an exception is a period of inflation. As money incomes of investors in bonds and mortgages remain fixed in the face of rapidly rising prices, their real incomes decline. A clever investor can avoid that embarrassment by shifting from bonds and mortgages to common stocks and direct ownership of real estate on the upswing of the business cycle, shifting back to bonds and mortgages as, or just before, depression sets in. Obviously such investment maneuvering requires more skill than a typical small investor possesses, and one error might easily dissipate the entire principal.

Corporate Bonds. A corporate bond is a promise by a corporation to pay a certain sum of money on or before a specified date with interest at an agreed rate. So far it would appear that a corporate bond is quite like a government bond, but in practice there are several differences. Chief among these is the security for repayment. While a corporate bond may be issued on the general credit of a company or upon the possibility of its earnings, such bonds usually are secured by a mortgage on all or a part of the corporate property. They are then designated as first or second mortgage bonds.

A second significant difference is that corporate bonds are repaid out of the proceeds of earning power. In the event that there are no earnings then the bonds are repaid out of the proceeds of the sale of property pledged as security. Whether or not a particular corporation earns enough gross income to meet its obligations is primarily a matter of good management, but may be the result of many other factors. Some of these may be within and others beyond control of corporation officials.

In view of these variations and uncertainties it is patently unwise for the average small investor to undertake the purchase of any corporate bonds. If he attempts to do so he will be as helpless as the average con-

sumer trying to buy a vacuum cleaner or an electric washing machine without some expert advice, while the amount of money involved would be considerably more. Particularly should he avoid bond issues of mining and oil companies. These ventures are unusually risky.[1] It frequently happens that some conservative corporate stocks are safer as to repayment of principal than certain types of corporate bonds. At this point it might be well to remind the average prospective small investor of the general rule that securities yielding more than $1\frac{1}{2}$ or 2 times the return on United States Treasury bonds are usually too risky. While a corporate bond promising a return of 7 per cent appears very attractive, a prospective buyer must remember that he is purchasing that larger return at the risk of losing his entire principal.

Corporate Stocks. Legally a share of common stock represents partial ownership and control in the corporation which issued it. In practice there are so many kinds of stocks that it is no longer possible to generalize concerning the status of stock ownership. Formerly it was possible to say that bondholders were creditors with no control in corporate management and no share in corporate profits, whereas stockholders were owners with voting control and no assured income, but with the prospect of a share in net earnings. In recent years many new kinds of stock have been issued. One investor may be the holder of a preferred share which gives him prior claim to participate in the net earnings of his company. Another investor may hold a 6 per cent cumulative preferred share which means that if he fails to receive his 6 per cent dividend one year other stockholders must forgo any share in net earnings the second year until he has received 12 per cent on his investment. Still another investor may hold a share of Class A nonvoting stock, which means that he has incurred all the risks incident to ownership yet has no voice in the control of the company.

As was stated in discussing corporate bonds, the income of a corporation is a function of several variables over which corporate management may or may not have complete control. It is quite certain at least that individual stockholders in large corporations have no adequate control over management. From an investment point of view they are in the position of having lent their capital to the corporation without any promise of repayment and without any promise of payment for the use of it. This is clearly a speculative venture in which the typical small investor has no right to engage. To him the loss of his principal is too serious to incur such a risk. The points on which information is necessary before one can make a wise decision concerning the advisability of pur-

[1] See Baarslag, Karl, *Robbery by Mail*, chap. 15, Farrar & Rinehart, New York, 1938.

chasing a certain stock are too numerous for a small investor to analyze adequately. He must have information concerning capitalization, whether or not there is sufficient working capital, whether the corporation is properly integrated, whether the management is capable, whether the management will protect the interests of stockholders or look only to its own advantage, and whether the corporation has adequate banking support.

This brief discussion leads to the conclusion that the small investor whose interests are under consideration should as a general rule avoid corporate stocks. This conclusion represents the consensus of opinion of writers on investment practice.[1]

Safeguards and Sources of Information

The Usual Sources of Information. From what has been said it might be concluded that no special sources of information need be suggested for the small investor. If he is to confine his investments to Federal or state government bonds, following the advice of his banker, he will not have much need for using those sources of information commonly available to investors. The reason for including this topic is that there are so many variations among individual investors and such a strong urge to mix speculation with investment that in spite of what has been said, not only here but in many other books, many investors who should confine their purchases to government bonds will not do so. If they insist upon entering the market for municipal, utility, or corporate bonds and possibly some corporate stocks, then the least that can be hoped is that, for their own sake, they will make use of some of the information available in the following sources. (1) *Kimber's Record of Government Debts*. This is issued annually and contains a description of national government loans. (2) *Moody's Manual of Investments*. This appears in five separate volumes: (*a*) Governments and Municipals, (*b*) Railroads, (*c*) Public Utilities, (*d*) Industrials, and (*e*) Banks, etc. The reader is given a key to bond and stock ratings which gives him at a glance the judgment of others concerning their desirability as investments. (3) *The Corporation Manual*, formerly issued as *Poor's Manual*. This is essentially the same as Moody's. (4) *The Commercial and Financial Chronicle* issues a state and city section which contains financial data on states and cities of the United States. In May and November the railroad and industrial supplement is issued, while the public utility section appears in April and October. (5) *Fitch Bond Book*, published annually by the Fitch Publishing

[1] For a suggested investment program confined to co-operative securities see Augustus, E. K., "A Complete Investment Program," in *Ohio Farm Bureau News*, p. 12, December, 1943.

Company of New York, contains concise information on all important bond issues. (6) Among government publications are certain volumes of the census reports such as *Financial Statistics of States* and *Financial Statistics of Cities*. For those interested in railroads the annual reports of the Interstate Commerce Commission contain valuable information. For those interested in bond issues of the Federal government the annual reports of the Secretary of the Treasury contain information on national finance and financial policy. (7) Among available periodicals some of the better known are *The Commercial and Financial Chronicle*, *Financial World*, *The Magazine of Wall Street*, *Barron's*, and the *Wall Street Journal*.[1]

Considerable discretion must be exercised in evaluating information obtained from these sources. Frequently the borderline between statement of fact and expression of opinion is difficult to locate. This is probably less true of annual publications than of periodicals. Prospective investors should beware of tips of all kinds, whether by word of mouth or by the printed page. There is documentary evidence that information which has appeared in certain financial journals in the past has not been entirely unbiased. During the operation of pools it was, according to the record, common practice to run articles in certain financial journals designed to make certain selected stocks appear attractive.

The Securities Act of 1933. Until 1933 the general rule in the sale of new securities as in the sale of most commodities was "Let the buyer beware." Heavy losses accruing to investors after 1929 resulted in extensive investigations by a Senate committee. These inquiries revealed amazing conditions in the investment securities market. The testimony and evidence made it clear that under the prevailing practices governing the marketing of any securities prospective investors were fortunate indeed if they escaped without incurring losses.

As a result of those revelations Congress passed the Securities Act of 1933, whose main purpose is to require those issuing securities to give more pertinent information concerning them. Senate committee evidence had shown that not all losses had been caused by fraud, as defined legally. In many cases investors were led to purchase securities on the basis of incomplete information. The act does not attempt to prevent investors from making unwise purchases. What it does attempt to do is to compel sellers to provide full information concerning the securities they have to offer.

Under the act it is necessary for every issue of new securities to be registered with the Securities Exchange Commission. That body examines the registration statement to ascertain if all terms of the act

[1] For a more detailed and complete list of sources of information see Sakolski, *Principles of Investment*, pp. 429–432.

have been met. If they have, a certificate is issued which permits the corporation to proceed with the issue of its securities. If not, the registration statement and prospectus which are available to prospective buyers must be amended so as to supply the omitted information. Until the terms of the act have been fully met, a corporation may not issue its securities. The act imposes civil liability on corporate officials and underwriters for any losses incurred by investors as a result of having relied upon an untrue statement of material fact in the registration certificate, or as a result of an omission of a material fact required by law or necessary to make the statements therein not misleading.

One illustration will indicate the important service being rendered by the Commission under this law. At a hearing before the Commission, the president and promoter of a gold-mining corporation organized in New Mexico admitted wide discrepancies between the facts and the registration statement which his company had filed with the Commission. It was revealed that property which had been purchased for $15,000 had been sold to the company for stock bearing a par value of $1,000,000 and had been included in the balance sheet at $4,000,000. It was revealed further that the mine had never been in production and that the so-called engineer who had appraised the property was a hotel clerk who had never had mining experience. Additional facts of this character were revealed in the hearing. As a result a registration certificate was denied and it is impossible to guess how many potential investors have been saved the loss of several millions of dollars by the work of experts on the Commission. There can be no doubt that the Securities Act of 1933 marks the beginning of a new period in the sale of new securities.

In the judgment of one competent authority, however, investors will get the kind of information and protection they ought to have only by providing it for themselves. This is essentially the conclusion reached by Mr. Bernard J. Reis, as a result of his study of investment practices over a period of years.[1] As a result of recommendations made by Mr. Reis, American Investors Union was organized as a non-profit group for the protection of the American investing public. Its stated objectives cover four broad fields of activity. The first of these is to examine the financial reports of selected companies, to demand explanations of doubtful items, to examine and report the trends of corporate devices, merger proposals, recapitalization, reorganization, or any other step which might affect adversely the interests of investors. The second major function is to analyze new issues of securities although they have been registered with the Securities Exchange Commission. This is because

[1] Reis, Bernard J., *False Security: The Betrayal of the American Investor*, Equinox Cooperative Press, New York, 1937.

the registration statements filed with the Commission are too technical to be understood by most investors. The third task is to act as a proxy for members of American Investors Union in selected cases, while the last function is that of suggesting and reporting changes in legislation designed to protect investors, holders of insurance policies, and bank depositors. American Investors Union sponsors a monthly publication entitled *Your Investments.* Information concerning this publication may be secured at the business office, 10 East 40th Street, New York. The annual subscription rate is $5. In *Your Investments* one will find helpful discussions of such topics as "A Diversified Portfolio for the Prudent Investor," "Insured Mutual Savings Bank—Best Buys for Savers," "The Best Buys in Investment Trusts," and "Real Estate and Mortgages in Wartime."

Summary

Investment involves the spending of money for the purchase of property desired for its income-yielding power. Ideally, a family head should have adequate insurance, a debt-free home, and from $1,000 to $3,000 in a bank before he attempts to buy investments, but many people enter the investment market without having made such provision. The difference between investment and speculation is difficult to draw, but in general the small investor may avoid speculative risks by purchasing Federal government bonds. Properly advised, he may buy certain state bonds, but he should shun all other types of securities if he wishes to conserve his principal. The usual sources of information may be helpful, but their conclusions should be checked carefully for impartiality and dependability. The Securities Exchange Commission, functioning properly, can protect gullible investors from predatory securities salesmen, especially if investors organize to supplement and re-enforce the work of the Commission.

QUESTIONS FOR DISCUSSION

1. When you spend money are you saving? Investing?
2. Is personal thrift still a virtue? What do consumer engineers think?
3. What percentage of your future income do you intend to save?
4. When you buy life insurance are you saving? Are you investing? Is your answer the same when you buy a home? An automobile?
5. Has anyone in your family ever incurred investment losses? What were the circumstances?
6. As an investor would you prefer a proprietary or a creditor status?
7. If the average interest being paid by the Federal government on its funded debt is $2\frac{1}{2}$ per cent, what rate of return can you, as an investor, expect to receive, with due regard to safety of your principal?

8. If you had a lump sum of $1,000 to invest what would you buy? In reaching a conclusion what sources of information would you consult?
9. If your budget provided for saving $16.30 a month how would you invest it?
10. If you anticipated a period of inflation, what shifts would you make in your investments?

PROBLEMS AND PROJECTS

1. Discuss the conclusions reached in this chapter with your father; to what extent have his savings and investment practices coincided with the recommendations made here?

2. Submit a report based on John T. Flynn's *Security Speculation*, or on *False Security* by Bernard J. Reis.

3. Choose two or more securities for comparison; on the basis of all available information decide whether they are good investments or whether they are speculative.

4. Write a short report on the meaning and practices of investment trusts.

5. Make a study of "guaranteed mortgages" and report your findings.

6. Prepare a chart showing the daily or weekly quotations on selected bonds or stocks for three or six months.

7. Check the recommendations of a financial journal with a particular security record; would you have gained or lost if you had followed the recommendations?

8. Assume you have $3,000 to invest. After deciding to play the stock market keep a record of your assumed daily or weekly transactions, including brokerage fees; after several weeks or months see how much of your $3,000 you have left.

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24

Producer Aids to Consumers

Consumers Need Help

Changes in Producer-Consumer Relationships. In an early chapter the manufacturing and merchandising methods of colonial times were compared and contrasted with present methods in some detail. During the colonial period buyers were better able to judge merchandise, and the personal relationship of seller and buyer created a situation in which fraud was difficult. The commodities for sale were of small volume and variety. Because of their simplicity it was easier to judge their quality. A larger proportion of the goods bought were made to order, and there was practically no selling pressure. Today the situation is altogether different. There are far more producers, producing more goods and marketing many of them under brand names, with much selling pressure and very much more impersonality in their relations with consumers.

How Producers Have Reacted to New Conditions. It is common knowledge among businessmen that ultimate consumers are generally unable to judge the quality of the things they buy. It is a matter of fact also that many hired salespersons are equally helpless in comparing the qualities of different brands of the merchandise they sell.

Classified according to their reaction to this situation, producers fall into three general groups. There are, first of all, a comparatively small number who seek to capitalize consumer ignorance by misrepresenting whatever they have to sell, to the point of fraud. The practices of such producers are well known, and evidence of their tactics has been given in preceding chapters, especially in Chapter 12.

A second and much larger group seek to profit from consumer ignorance by using brands, trade-marks, and advertising. It is their purpose to lift their products out of the competitive field by attempting to make consumers think that they are the best to be obtained. Large amounts of money are spent in advertising to build up good will and to develop consumer habits which will make profits for these producers.

The third group take a somewhat different attitude. Realizing that consumers are quite unable to compare the quality of numerous brands of merchandise, they attempt to provide special assurances to their customers that their products are as good as they are claimed to be.

Brands and Trade-Marks. To those of us who have been reared in a trade-marked world it is difficult to imagine an economic system in which the market is not filled with thousands of trade-marked commodities. There are, of course, many people who can recall the general store which sold the greater part of its merchandise in bulk without any trade-mark designation. Sugar, navy beans, flour, and many other such items were sold out of common barrels or bags which simply carried the one word designating the product contained therein. If one were to trace merchandising methods back still further it would be found that larger numbers of commodities were manufactured and sold without trade-marking. Why, then, has this modern device been adopted so completely? The trade-mark, as we know it, is an outgrowth of modern methods of production which involve the making of goods in anticipation of demand and their fabrication by machine methods in large factories, which entails heavy overhead costs. Producing under these circumstances, the modern manufacturer has been driven to adopt the two expedients of trade-marking his products and then of advertising them. His objective is to lift his merchandise out of competition so as to create a fairly steady demand which will enable him to reduce his unit costs by spreading his overhead among a larger number of units. It is significant to note that nearly the whole structure of modern advertising is based on the use of trade-marks. If it were not possible to identify merchandise by this means it would be impossible to advertise the products of a particular company. A flour miller does not advertise merely flour, but instead extols the virtues of his particular flour which is identified by a name or mark.

The nature of these trade-marks is too well known to require description. For the most part they consist of words or designs that have no meaning nor any necessary basis in fact. One may contrive almost any kind of design, or coin a new word. Some years ago the Chippewa Milling Company, operating in Minnesota, desired to copyright the trade-mark "Prize Medal Flour." In order to meet the copyright laws it was necessary to show that a prize medal had actually been awarded to the company for the particular flour to be sold under that name. In order to meet that requirement a contest was arranged at the local county fair, in which the Chippewa Milling Company entry won the prize medal. Having thus met the legal requirements the company was permitted to make use of the brand name and for many years sold flour under that mark.

It is difficult to dissociate the nature of trade-marks from the adver-

tising which is designed to make them known to consumers. Millions of dollars have been spent through advertising media for no other purpose than to keep the brand name or trade-mark in the minds of consumers. Such advertising may make no claims for the superior quality of the trade-marked merchandise or for its lower price. The objective is simply to impress the name so deeply on the buyer's mind that when a purchase is to be made he will not ask simply for a sack of flour, for example, but rather for Prize Medal. There is, however, an increasing tendency in certain areas for the advertising copy to present fantastic claims of superiority over all other similar products.

There can be little doubt that the system of brands and trade-marks has proved a valuable aid to manufacturers and distributors. Once a brand or trade-mark has been adopted and registered, a property right accrues to the company in whose name it is registered. This can be defended successfully in court against encroachment by competitors. Having been granted the exclusive right to use a certain word or design to identify his merchandise, a manufacturer may then proceed to spend large sums in advertising it to consumers. The belief is that consumers will develop purchasing habits which will guarantee their patronage in advance. If this can be accomplished the manufacturer has lifted his product out of competition and is assured a fairly steady market at fairly steady prices which may be higher than prevailing competitive prices. In recent years there has been a strong movement to enable the manufacturer to set the minimum price at which anyone may retail his trade-marked product. The significance, for consumers, of this new development will be examined in Chapter 27.

The value of trade-marks to consumers is less easily established. They give no information concerning quality of the merchandise they represent. In fact, the Trademark Act does not permit the registering of words or devices which seek to describe the goods or to indicate their quality. It is contended that trade-marks are a guide to quality because the manufacturer will stand to lose patronage and repeat sales unless his product is satisfactory. Carefully considered, what this argument really contends is nothing more than that the merchandise must be satisfactory to the consumers who buy it. Remembering that most consumers cannot judge the quality of the things they buy, it is readily seen that the mere fact that they purchase a certain brand is not evidence of its high quality. There may be 206 (see page 290) other brands of equal or superior quality and it is quite possible that there is merchandise available in bulk form which is as good as, or better than, the branded product.

The trade-mark provides no information as to comparative price,

and those manufacturers making the greatest use of this device are inclined to minimize price in their advertising. It is quite possible that similar merchandise carrying other trade-marks or no trade-mark can be purchased at a lower price.

It may have been true at one time that trade-marked merchandise was a useful device to consumers in that it saved them time when they entered the market place. The argument was that having made purchases of a particular trade-marked product and having found it satisfactory they did not need to spend time shopping around nor need to run the risk of making an unsatisfactory purchase by trying some other unbranded and unknown commodity. Today the situation is quite completely changed. A prospective buyer entering the market finds himself confronted with scores of brands covering particular products. How is he to know which of the many brands of flour, tooth paste, or gasoline is best for his purpose? As now used, a trade-mark is as likely to confuse as it is to help.

An implied argument in favor of trade-marked merchandise is that once the buyer has made a satisfactory purchase he can be assured of uniform quality in the future. But who is to give the assurance other than the manufacturer? While it may be true that the quality of some products can be maintained at a desired level of uniformity, it is true also that other products can and do vary considerably. Evidence has been presented in Chapter 13 showing how gasoline may vary in quality. In the same chapter even more evidence was presented showing how unreliable trade-marks are as guides to quality and price in the purchase of canned goods.

The services of Consumers Union and Consumers' Research are based almost entirely on the use of brands and trade-marks. Without them these organizations would be unable to identify merchandise so as to indicate to their members how to secure a good quality product at a fair price. Even such an organization as Cooperative Distributors trade-marks most of the merchandise distributed by it with the identifying letters CD, and consumers' co-operatives are increasingly stocking the CO-Op brand. While some companies owning registered trade-marks spend millions of dollars to induce consumers to purchase their particular products, Consumers Union and Consumers' Research spend only a few thousand dollars to compare competing brands and to inform their members as to the truth concerning comparative quality and price.

Labels. The increased use of labels results largely from the increased use of advertising and of packages. Their use is closely associated with trade-marks. Indeed from the producer's point of view there may be very

little difference between labels and trade-marks, a label frequently being nothing more than a device for applying a trade-mark to the product.

The form which a label takes varies with the commodity on which it appears. A label may be stamped on, as in the case of oranges and unpackaged meat, or sewed on, as is the custom in labeling clothing. Labels for products contained in bottles or tin cans are usually stuck on the containers, while they are printed on the wrappers of some products such as candy and chewing gum. A very large proportion of merchandise is retailed today in packaged form, the labels being pasted or printed on the package.

The information which a label bears varies considerably. Frequently it bears nothing more than a trade-mark. Sometimes it contains nothing more than the name of the manufacturer, whose address may or may not be included. Not uncommonly labels carry directions for use, claims for what the product will do, or statements of quality. A fairly recent development is the practice of stating on the label when the merchandise was packed or the time period within which it should be used. In many cases the law requires that the quantity contained in the package be shown by a statement of its weight, measure, or count. With the exception of labels covering foods, drugs, cosmetics, and woolen goods entering interstate commerce,[1] statements on labels need not be factual. In many cases they are or may be positively deceptive. Better Business Bureaus are constantly on the trail of firms which label merchandise as being imported when it is manufactured domestically, or as containing materials in whole or in part which it does not contain.

The value of labels to producers is very similar to that of trade-marks. In addition to carrying the trade-mark itself, labels may contain additional printed matter which may attract consumers. This is not likely, however, for in general consumers are much more easily persuaded by advertising. In fact, it is questionable to what extent consumers read the statements printed on labels, particularly if they run into any length or are inclined to be technical. There are several special uses for labels, whose value to producers is evidenced by their rather widespread adoption. For example, a union label indicating that the product carrying it has been manufactured under satisfactory labor conditions by workers who are members of an organized union, is a device which has been used with success by some manufacturers, the sale of whose products is thereby increased in centers where organized workers constitute an important market. A similar special label is that sponsored by the Consumers League. The appearance of this label on merchandise is evidence that

[1] For the special provisions regarding labels covering these products, see Chapter 28.

the manufacturer has employed no children and that the conditions of work, rates of pay, and length of the working day are satisfactory in his plant. The use of the label was given considerable impetus in 1933 and 1934 during the period of the National Industrial Recovery Act. Strong pressure was put on manufacturers to label their products as evidence that they had been manufactured under N.R.A. codes. Equally strong pressure was then put on consumers to encourage them to purchase only merchandise carrying N.R.A. labels. Although the National Recovery Administration has long since passed out of existence some manufacturers still use code labels, and a movement is being sponsored by the Consumers League to encourage an even greater use of labels to identify merchandise produced under satisfactory conditions. Another special type of label is that used by many manufacturers to indicate that a particular organization or society has vouched for the quality of their products. The *Good Housekeeping* Seal of Approval, which will be discussed in the latter part of this chapter, is one such label. Others are those issued by the American Dental Association to manufacturers of approved dentifrices, and by the American Medical Association to manufacturers of approved foods and medicinal preparations.

It is difficult to indicate the value of labels to consumers. In the case of foods, drugs, cosmetics, and woolen products entering interstate commerce the label contains factual information upon which the consumer can rely. Misstatement or misrepresentation opens the manufacturer to prosecution and penalty. Experience of the Food and Drug Administration indicates that consumers pay scant heed to labels. This generalization applies whether the labels contain reliable factual information or positive misstatement. The greater part of any information which consumers may secure is derived from advertising.

For other merchandise the label, like the trade-mark, is of doubtful value. It is certainly no reliable guide to quality nor an assurance of uniformity. The actual printing of labels costs but little and the superlative words which many of them contain cost nothing.

The presumption, however, is that only reliable manufacturers will use identifying labels. Their objective will be to secure repeat sales, and in order to accomplish that it will be necessary that the labeled merchandise satisfy buyers. In this way it is the hope of the manufacturer that his label will become a guide which prospective buyers will follow to their satisfaction and to his gain. To the extent that labels actually contain reliable factual information on which consumers rely, they may serve this purpose and thus benefit both consumers and those producers who use them. To the extent that labels depart from this high standard, consumers find them of little use.

In the years just before the attack on Pearl Harbor there was a growing interest in the use of labels by certain trade associations and by some firms as merchandising devices. The National Retail Dry Goods Association, for example, made a survey to find out what kind of information customers and retailers wished to have on dry goods. The report began by accepting the premise that the consumer wants more information about the merchandise she buys. The real question was specifically what information was wanted. The survey disclosed that for dresses consumers wanted the following information and their judgment of the relative importance of each item is indicated by the order in which it is listed: Most of the buyers wanted first of all instructions for washing or cleaning; the remaining items on which information was desired were the kind of material, size, instructions for special care, weighting, quality, grade, construction. Similar preferences were disclosed for a wide range of drygoods.[1]

Realizing that although the firm producing Westinghouse appliances was aware of the design, manufacture, inspection and pricing policies, consumers confronted with many brands needed more precise information, Westinghouse announced a policy of attaching informative labels to its 1941 electrical appliances. Under the title "Information for Consumers" the label for a fan gave factual information concerning over-all dimensions, color and finish, motor, oscillator, arc of oscillation, blades, air power, current function, wire guard, swivel joint, switch, and the seller's guarantee. In the remaining pages of the little booklet, these terms were explained and discussed at greater length and instructions for use and care were presented. It seems needless to say that the more of that kind of information consumers are given, the more intelligent choice they can make.

Guarantees. The guarantee is an outgrowth of the economic and legal doctrine, originating in the eighteenth century, known as *caveat emptor.* In practice and in law an injured or victimized consumer was simply reminded that upon entering the market place the buyer should beware. Sellers' claims as to quality were discounted as merely trade puffing. In a situation where the consumer had no recourse at all it was logical that some more scrupulous producers would develop some device for assuring prospective buyers that they could rely on the definite statements made by the seller concerning quality. This device became the guarantee. Its purpose and its effect were to give the guarantor a competitive advantage. When this was realized, less scrupulous businessmen freely adopted the guarantee, but when buyers called upon them to

[1] National Retail Dry Goods Association, *Merchandise Labeling,* 101 West 31st Street, New York, 1938.

live up to their guarantee they failed to respond. The next step was a legal definition and interpretation of the meaning and use of guarantees. The result has been the growth of a body of legal doctrine which renders the guarantee comparatively harmless.

In modern practice guarantees may take several different forms. Some firms adopt general sales policies covering all goods sold by them. This is the practice of some retailers, particularly large department stores that have adopted the policy as stated in the slogan that "the customer is always right." In this form, while there is no specific guarantee covering every transaction, there is an implied and sometimes an express guarantee that all transactions must be satisfactory to the customer; that dissatisfaction, regardless of its cause, will be remedied by the substitution of satisfactory merchandise.

A second form is that of specific warranties of certain goods such as automobile tires or household appliances. In some cases these guarantees are reduced to writing and a copy is filled out to be retained by the purchaser. This type of guarantee is much more restricted than the one described above. The rights of the purchaser are stated strictly and technically in written form. Beyond that they do not go.

Another type of guarantee is that which seeks to assure the customer on some specific point. A manufacturer may warrant, for example, that his product is one hundred per cent wool or that the color of the fabric will not fade. These specific warranties may be substantiated by a promise to refund the purchaser's money in case the merchandise does not meet the terms of the promise. A more common method is that of providing adjustment under which the customer is charged a proportional amount for the use which he has already had from the product. In other cases there is no definite policy in meeting customers' complaints and in all cases there is always a strong probability that a dispute will arise as to whether or not terms of the guarantee have been met.

The value of guarantees to producers depends pretty largely upon the extent to which those who make them follow a liberal policy of living up to them. If customers find that a particular producer not only makes but respects a fairly liberal guarantee of his products, they may quite likely pay higher prices and will be even more likely to make all their purchases from him. If the manufacturer's merchandise is good enough to warrant his guarantee, then of course he has nothing to lose and a great deal to gain in following such a policy. Unless, however, he is willing to live up to the promise formally made to his purchasers, the guarantee will prove of slight value to him because it will not draw or maintain permanent patronage. Unfortunately for reliable guarantors,

there are many unreliable and some unscrupulous dealers who use the guarantee as a competitive device without having any intention whatever of meeting its obligations.

In examining the value of guarantees to consumers it is evident that the question turns entirely on the reliability of the guarantor. This is particularly true because in practice and in law the consumer has very slight recourse. The guarantee, for example, is generally valid only between the buyer and the person or firm from which he buys. This means that a manufacturer's guarantee is of no benefit to a consumer unless it is definitely made by the manufacturer's retail distributor. Assuming that such a guarantee is made, and assuming further that the guarantor contests the claim of a dissatisfied buyer, the latter must institute suit in a court of law to recover damages. Businessmen know that buyers are not going to undertake legal proceedings unless the amounts involved are large. Such cases are likely to be rare, because the generally accepted legal rule is that the buyer may receive as damages only the difference between the actual value of the article and what its value should have been as warranted. If a buyer has suffered physical injury as a result of consuming a product, he may sue the distributor and in some cases the manufacturer for negligence, but this right accrues to him whether or not a guarantee has been made.

A new development designed to assure purchasers that guarantors mean what they say, is the device used by a certain dress manufacturer. Under this plan each dress is dated by a stamp at the time of sale and given a one-year guarantee covering quality of fabric, fastness of color, washability, shrinkage, and workmanship. The guarantee provides that within one year failure of a dress to give satisfaction will entitle the buyer to a replacement.

Generally speaking, department stores and mail-order houses have developed the reputation of being reliable guarantors. It is their policy to follow the practice of satisfying the customer completely even though such procedure may entail recognition of some claims that are not valid. In this connection it is significant to observe that department-store customers having charge accounts have an invisible leverage which frequently assures them a more satisfactory adjustment than if they paid cash.

Although guarantees are closely related to the use of trade-marks and labels, it may be asserted that in general retail buyers do not place much reliance on them. Experience has shown that guarantees are so easily made that they are hard to enforce. While guarantees are not in themselves informational, they may vouch for the validity of information contained on a label or in an advertising statement. Most of them are so

vague or so general as to be easily evaded and consequently quite useless to the ultimate consumer.[1]

Other Types of Producer Aids

Testing Laboratories. Evidence that the profit motive impels some manufacturers to cut corners on quality is found in the increasing number of laboratories maintained not only by the purchasing departments of large business firms but also by the purchasing departments of large retail stores. Illustrative of the latter type is the Bureau of Standards maintained by R. H. Macy and Company, New York City. Originating in 1927, the Bureau undertook a fourfold program which includes analysis and comparison of the offerings of manufacturers, testing for the purpose of determining performance and durability, examination of materials returned by customers for adjustment, and collection and classification of information received for the standardization of merchandise. During the first 16 years of operation 350,000 different specimens were tested. The number of actual tests conducted was estimated to have been approximately 3,000,000. The Macy innovation has been emulated by other stores, including Bamberger's, Wieboldt's, Kaufman's, and Bloomingdale's, by mail-order houses such as Sears, Roebuck and Montgomery Ward, and by the Piggly-Wiggly chain.

Among the frauds discovered in the Macy laboratory were a piece of cowhide masquerading as alligator skin, a "cure-all" liniment which proved to be impure chloroform, washable articles which faded, stained, or shrank excessively, "sunfast" curtains which faded almost immediately, "borax powder soap" which contained no borax, and a reducing bath powder composed mostly of starch with a dash of borax and soda.

Increasingly the findings of Macy's Bureau of Standards are coordinating the activities of the purchasing, advertising, and retail sales departments. Store buyers are guided by the results of laboratory tests. In this way the retailer assumes a definite responsibility for quality and performance. This practice supplements the store's guarantee policy, rendering it much more effective and reliable as well as less expensive. Merchandise is advertised factually, all advertising being subject to review by the director of the Bureau. Indicative of the censorship exercised, advertising copy which announced a "3 Piece Knitted Kid Angora Suit" was changed to read "3 Piece Knitted Suit of Angora and Wool. The skirt and jacket are all mohair. The blouse is of wool trimmed with rabbit hair."

[1] For further information on guarantees from the consumer point of view see Weiss, William F., *How to Keep out of Trouble*, chap. 30, "Beware of Puffing and Sales Talks," Doubleday, Doran & Co., Garden City, 1942; for a brief discussion of guarantees from the seller's point of view see *Printers' Ink*, April 19, 1940, pp. 83–87.

The advantage to the consumer of such a co-ordinated merchandising policy is obvious. In this case and in similar cases where retail distributors are following these methods they are performing a genuine service for their customers. It must be remembered, however, that both absolutely and relatively the number of such testing laboratories operating to the direct benefit of consumers is very small. In at least one case it is reported that the "laboratory" is a makeshift affair operated on a limited scale by an independent commercial firm, its purpose apparently being to serve as a sales promotion scheme. Moreover, in those few cases where such service is rendered the ultimate cost is borne by consumers in the prices they pay. Operating expenses for a testing laboratory are included with all other costs of operating a business and are deducted before a firm calculates its net earnings. This means then that a store such as Macy's is not performing its testing service gratuitously although it is performing it voluntarily, that is, without compulsion. When the merchandise is offered for sale no definite statement appears in connection with it that it has been tested for certain qualities and found acceptable. The presumption is that such tests have been made but there is no evidence that all merchandise offered for sale is tested. Nor does the customer have any assurance that the price indicated on the tag is fair. Again there may be some presumption that differences in price indicate differences in quality, but there is no positive statement to that effect.

Customer Research. Much more modest and limited in scope are the customer research programs of General Motors Corporation, and the Scott Paper Company's Department of Consumer Representatives. The General Motors plan is described as an attempt to maintain personal relationships in modern industry and to discover customers' likes and dislikes. The research is limited to automobiles and seeks customers' suggestions, chiefly on body design. The Scott plan entails door-to-door interviews with consumers to ascertain what they want in tissue towels and toilet tissue. Obviously these manufacturers are attempting to discover what added features will help to sell their products. There is no effort to cover a broad field or to render a buying aid to consumers. Rather it is the consumers who are rendering aid to the manufacturer. It is helpful to them only in the sense that it gives them an opportunity to tell a particular manufacturer what features one would like to see in his product. Reduced to these terms it is obvious that this device is of very limited if of any use to consumers.

These limitations are clearly illustrated in the practices of many large manufacturing and distributing firms which test their products very thoroughly in their own laboratories and on their own proving grounds, but fail to make the results of those tests available to consumers. One

such firm ran a test comparing its refrigerator with 9 other popular brands. Its findings were compared also with those of Consumers Union and Consumers' Research. In some respects brand "X," the testing firm's product, compared very favorably, but in other respects it was found to be at a competitive disadvantage. For example, the report recommended that the fan should be eliminated, that the freezing unit should be more favorably located, and that the compressor should be constructed so as to operate more quietly. The continuance of an undesirable hazard in the freezing unit was also noted and deplored. While consumer buyers could get such information from Consumers Union and Consumers' Research, they did not have opportunity to see the results of the tests made in the distributor's own laboratory, although the findings were quite similar—in fact, they were identical on some points.

Informational Pamphlets. In general it may be said that all producer efforts to aid consumers are designed to create good will. A far less elaborate and less expensive device is the publication in various forms of factual information to serve as a guide for consumers when they set out to purchase certain commodities. Several department stores in different cities have made use of a series of leaflets entitled "*How to Judge Values.*" These leaflets were prepared by the Household Science Institute, described as an independent, nonprofit research organization. Covering some 22 different drygoods items, the leaflets are concise and informative.

Considerably more comprehensive are the *Better Buymanship* bulletins published by the Household Finance Corporation. This series, numbering twenty-seven bulletins, covers a wide range of commodities which consumers purchase frequently. Among the broad classifications covered therein are foods, clothing, house furnishings and appliances, and automobile accessories. The Corporation maintains a Department of Research which prepares and edits the bulletins. On the basis of careful examination it may be said that they are not only comprehensive but accurate and reliable. A complete set might well be included on the reference shelf of every careful consumer.[1]

Honest Advertising. The possibilities of honest, informative advertising as an aid to consumer buyers were discussed at some length in Chapter 10. These is no need to repeat the general argument at this point nor to do any more than to remind the reader of the general conclusion that if advertising statements were made reliable consumers would gain and so would businessmen. Some efforts have been made in that direction, but in general commercial advertising has a long way to

[1] For additional information on *Better Buymanship* bulletins, and an evaluation, see page 341.

go before it will provide consumers with any considerable reliable information such as that presented in the informational pamphlets described above.

Special Devices Designed to Aid Consumers

Good Housekeeping Guaranty Seal. Among the oldest and most elaborate of services designed to aid consumers are those of *Good Housekeeping* magazine. Back in 1912 William Randolph Hearst conceived the idea of establishing a Good Housekeeping Institute and a Good Housekeeping Bureau of Foods, Sanitation, and Health. The ostensible purpose of these agencies was to aid and protect consumers. In order to strengthen consumer confidence in the project, Dr. Harvey W. Wiley was appointed director, serving in that capacity until 1929.

The general plan of these agencies was that products advertised in *Good Housekeeping* magazine had been tested and approved. The tests were conducted without charge to the manufacturer and it was claimed that a large percentage of tested merchandise was rejected. With the exception of certain kinds of goods, a manufacturer whose product had been accepted was permitted to use the *Good Housekeeping* Seal of Approval in his own advertising and as a label attached to his product. The label was offered to purchasers as assurance that the product was as represented. Magazine readers were guaranteed that if a product advertised in *Good Housekeeping* were found to be unsatisfactory it would be investigated and, if proved defective, would be replaced or the customer's money refunded. The Good Housekeeping Institute limited its activities to mechanical devices and articles of household equipment. The Good Housekeeping Bureau limited its activities to the investigation of foods, drugs, and cosmetics.

In August, 1939, the Federal Trade Commission served a complaint upon Hearst Magazines, Inc., charging it with the use of unfair methods of competition in commerce and unfair or deceptive acts and practices in commerce. After nearly two years the Commission announced the following findings: that from 1920 to 1939 *Good Housekeeping* had operated a shopping service represented as free "when in truth and in fact respondents received a commission of from 5 per cent to 7 per cent from the sellers of the merchandise purchased through such service"; that *Good Housekeeping* represented that its guaranty was unlimited when in fact it was not; that whoever wished to use the Seals was required to purchase them and all plates and certificates from *Good Housekeeping;* that the tests "generally were not sufficient to insure the fulfillment of the claims made for such products. In some instances seals of approval with respect to services or commercial offerings have been issued without even an

adequate preliminary investigation . . . "; that "many of the advertisements appearing in *Good Housekeeping* magazine contained false, deceptive, and misleading statements and representations . . . " Holding that Hearst Magazines had violated the Federal Trade Commission Act, the Commission issued an order to cease and desist from representing in its advertising that statements are true when in fact they are not; permitting the use of seals of approval unless adequate and thorough tests actually have been made; representing that any product advertised in *Good Housekeeping* is guaranteed by *Good Housekeeping* unless such guarantee is without limitation, or if limited that such limitations are clearly stated.[1]

In its issue of October, 1941, *Good Housekeeping* announced its new Guaranty Seal which contains the statement "replacement or refund of money guaranteed by *Good Housekeeping* if defective or not as advertised therein." The Good Housekeeping Institute and the Good Housekeeping Bureau were discontinued as were all other seals. The change was announced as having being required for reasons of national defense.

Good Housekeeping has long been pre-eminent in the field of magazines for women and there can be no doubt that thousands of housewives have used the various seals of approval as one of their guides in buying. Results of a market survey made in Philadelphia and Bridgeport, Connecticut, indicated that of 2,097 women 60 per cent selected a brand of merchandise bearing the *Good Housekeeping* seal. When questioned further, however, it was found that the seal was not the main or the only reason for their choice. The seal was mentioned as a reason for preference 382 times, can size 413 times, and brand 523 times.[2]

Some consumers who question the integrity of an organization such as Consumers Union or Consumers' Research accept the recommendations or the guarantee of *Good Housekeeping* without question. Yet there are some questions which should arise in their minds. Assuming that the tests to which products are subjected are valid, the seal simply says to prospective buyers that the article is probably all right in performance. It does not indicate that it is the best available article. The consumer has no knowledge of the standards by which products are tested. If standards were set very high the number of potential advertisers would be reduced and the gross income of the magazine might decline.[3]

Another question on which the Guaranty Seal throws no light is the comparative value of the product. It may very well be that the product

[1] Federal Trade Commission, *Decisions*, vol. 32 Docket 3872, May 13, 1941, pp. 1440–1453.
[2] *Tide*, April 15, 1943.
[3] See also Temporary National Economic Committee, *Hearings*, Part 8, *Problems of the Consumer*, p. 3380.

has been tested and found to be of fairly high quality which justifies its advertising claims. At the same time it may be true also that the price which the consumer is expected to pay is higher than it should be.

Neither does the Seal give any indication of the conditions under which the product was manufactured.

This particular device for aiding consumers differs from others considered in that the organization sponsoring the service is a producer who stands midway between the manufacturer and the consumer. On the one hand he stands to gain from increasing advertising appropriations and on the other hand from an increased subscription list. Incidentally the larger the subscription list the higher the advertising rates which can be charged. The price which subscribers pay for *Good Housekeeping* magazine can scarcely cover printing and postage costs. If these statements present an unbiased picture of the situation then those who depend on the Guaranty Seal might very well ask: "Can *Good Housekeeping* magazine serve two masters?"

Producers' Joint Efforts

Efforts to Secure Truth in Advertising. The brief discussion which follows includes a number of activities designed not so much to aid consumers as to protect the more scrupulous from the less scrupulous businessmen. It follows, of course, that any success along these lines will benefit consumers as well as ethical producers. Our preceding discussion of advertising has established the need of developing higher standards. The problem of securing truth in advertising is one which has engaged the attention of many persons for a number of years. As far back as 1913 the Associated Advertising Clubs of the World undertook a campaign to increase truthful advertising. This is another means of saying that they undertook to reduce the amount of misrepresentation and fraudulent advertising. An outgrowth of this activity was the development of Better Business Bureaus which are to be found in most large cities. These Bureaus operate to protect most businessmen and consumers from the predatory activities of a small but persistent group. One of the latest groups to undertake a housecleaning campaign is the Proprietary Association. The new leaders of this organization are attempting to raise the standards of practice among manufacturers and distributors of patent medicines.

Self-Regulation in Baseball and Movies. In the 1920's scandals in professional baseball involving "throwing" of games, and in the movies involving the personal lives of actors and the low standards of pictures, resulted in purging efforts under the czaristic control of Judge Landis and Will Hays. These moves were prompted by the loss of, or the fear

of losing, public interest and patronage. There can be no doubt that in both baseball and movies standards have been raised from the low plane to which they had fallen, but this is not to say that they have been raised to a desirable level. It cannot be denied that the results desired by producer interests have been realized, for certainly both industries gained in public favor.

At this point attention may be called parenthetically to a special kind of producer aid in the form of reviews of plays, movies, and books published in newspapers and periodicals. As conducted by some editors these reviews serve as useful guides to prospective consumers, but in other cases the sinister influence of the advertising manager is justifiably suspected.

Trade Association Standards and Testing Laboratories. Until recent years trade associations were concerned primarily with problems of production, including labor relations and price control. There is a growing tendency for such associations to study the problems of distribution and selling. This means that they are becoming concerned with what might be called consumer relations, and in a few cases efforts are being made to establish standards and facilities for testing merchandise. Among groups operating such laboratories are the National Retail Dry Goods Association, the American Gas Association, and the Edison Electric Institute. Quite clearly it is to the advantage of producers of gas appliances to offer safe, standard, and economical equipment; otherwise consumers would be likely to turn to some other form of heating and cooking device as they have turned almost completely to another form of lighting. This suggests the most serious limitation from a consumer point of view upon this type of joint promotional consumer activity. Whereas competition formerly operated between independent firms, the trade association coordinates the firms in an industry, and competition assumes a new form between all the firms of one industry and all those in another. If the producers of gas appliances do succeed in offering to consumers desirable new devices the producers of electric appliances immediately confuse consumers with advertising which extols the virtues of electricity and either openly or impliedly stresses the dangers of using gas. In other respects the operations of such associations are likely to be against consumer interests. For example, the National Electric Light Association, predecessor of Edison Electric Institute, was a persistent and powerful lobbyist against public ownership. It has been suggested that one of the major concerns of trade associations is to establish what they call price stability, which means high or higher prices for consumers.

An illustration of associational activities beneficial alike to producers and to consumers is found in the National Consumer-Retailer Council.

This was organized as a result of a decision on the part of consumers and retailers to bring their problems to each other in a constructive effort to solve them. Leading retailers have reported that their efforts to give consumers the information they want have resulted in more sales and greater profits. The Council has emphasized particularly the greater use of informative labels.

Professional Societies Benefiting Consumers

American Home Economics Association. The work of the American Home Economics Association is largely educational and indirect. Its contacts are chiefly with teachers of home economics in secondary schools and colleges, and through them with the students in those institutions. Comparatively, there is very little direct relation between the Association and adult consumers. Through the publication of its *Journal* and *Consumer Education Service* and through its legislative activities this Association has become an important channel for conveying new information. If one holds to the belief that adult consumer habits are too deeply ingrained to be altered then one can place even more importance on the work of the American Home Economics Association, for it is dealing always with the young people, particularly girls, who will be the buyers for the succeeding generation. If it is true that in them lies the chief hope of promoting consumer welfare then this organization might well be considered one of the most significant.

American Dental Association. The Council on Dental Therapeutics was established by the American Dental Association in 1930. Of the 10 members 5 are dentists and 5 are active in medicine or chemistry. No member of the Council receives any financial remuneration for his services. "The primary aim of the Council on Dental Therapeutics is the steady improvement of the dental health of the people of the United States." Toward that end the Council seeks to protect the profession and the public against fraud or imposition, undesirable secrecy, and objectionable advertising of dental drugs and cosmetics. Its activities include testing and acceptance of therapeutic materials used by the profession; collection and dissemination of knowledge helpful both to the profession and to the public; co-operation with ethical manufacturers and distributors; and the testing of products and their performance. Products which meet the published requirements of the Council and are advertised honestly may be awarded the Seal of Acceptance. The Seal, however, does not signify a recommendation; it simply means that the article bearing the Seal was not in conflict with the Council's rules at the time of consideration. Dentifrices are accepted for one year. For the information of the public, the Council provides, without charge, a list

of acceptable dentifrices as well as informative articles on mouth washes, denture cleaners, and denture adhesives. Through its Bureau of Public Relations, the Association provides also, without charge, a list of dental health educational material.

American Medical Association. The organization of physicians called the American Medical Association performs dual services of education and testing. Unlike the American Home Economics Association, its work is to a large extent directly with adult, lay consumers. While the *Journal* it publishes is primarily for the benefit of practicing members, some of its space is devoted to the findings of the Bureau of Investigation and of the Committee on Foods. The educational program is expanded by the publication of *Hygeia* in popular style. Certainly every home that has a *Good Housekeeping* should have *Hygeia* also.

For many years the Bureau of Investigation has made searching inquiries of quacks and nostrums. Results of these investigations were first published in the *Journal* and were later assembled in a bound volume in 1911 entitled *Nostrums and Quackery*. Ten years later a second volume was issued, containing the results of investigations conducted during the preceding decade; and a third volume appeared in 1936. Each issue contains the results of current investigations. The following summary of an investigation of Dilex-Redusols indicates the straightforward, unequivocal statements characteristic of the Association's reports.

> "The postal authorities found the officers of the Dilex Institute, owner of the Redusols business—President William H. Door, Vice-President Maybelle Ryerson, and Secretary-Treasurer Dorothy T. Simms—to be the perpetrators of a scheme for obtaining money through the mails by means of false and fraudulent pretenses, and recommended that a fraud order be issued. The Postmaster General closed the United States mails to these concerns on January 11, 1936.
>
> "The postoffice inspectors are to be congratulated on bringing to a close this particular vicious piece of quackery—an exploitation directly to the public of a secret nostrum for reducing, which obtained such effects as were secured primarily by its content of dinitrophenol, a drug already established as potent for harm."[1]

Monthly summaries of the work of the Food and Drug Administration are drawn from *Notices of Judgment* and published in the *Journal*. Likewise, monthly summaries of the work of the Federal Trade Commission and of the Postoffice Department are summarized in the *Journal*.

The Council on Foods and Nutrition of the American Medical Association was created to prevent and discourage "unwarranted, incorrect or false advertising claims in the promotion and merchandising of food

[1] American Medical Association, *Journal*, May 2, 1936, p. 1,587.

products." The Council considers foods and food advertising and those that appear to conform to its requirements are accepted by the Council. Formerly available to the processors of all prepared foods, the Council has recently restricted its attention to special purpose foods. Those which meet its standards are permitted to display the Council's Seal of Acceptance on food packages and in related advertising. Foods submitted for analysis are accepted or rejected and the results published in the *Journal*. For example, the H. J. Heinz Company of Pittsburgh submitted "Heinz Strained Applesauce—Sugar Added" for analysis. In publishing its acceptance the Council on Food and Nutrition published the following analysis:

> "*Analysis* (submitted by manufacturer): Total solids, 16.2%, total sugar as sucrose 12.8%, reducing sugar as invert 8.9%, acidity as citric 0.38%, protein (N × 6.25) 0.20%, fat (ether extract) 0.05%, crude fiber 0.7%, ash 0.2%, total carbohydrates other than crude fiber (by difference) 14.7%, calcium 44.0 mg. per kilogram, phosphorus 32.0 mg. per kilogram, iron 1.5 mg. per kilogram, copper 1.7 mg. per kilogram.
>
> "*Calories*—0.5 per gram; 14 per ounce."[1]

It will be noted that these investigations pertain only to quality, no effort being made to express judgment as to fairness of price quotations.

In 1939 the Council assembled a large number of its analyses in a volume entitled *Accepted Foods*. Testing and rating are confined to processed foods. A product is accepted for a period of two years during which the manufacturer or distributor agrees to maintain the food and all advertising concerning it according to the rules and regulations of the Council. At the end of the two-year period the product and its advertising must be submitted for further review. To be accepted the manufacturer must provide all the facts regarding the preparation of the food and the product must comply with all requirements of the Food and Drug Administration. Moreover, its identification label must be informative and its advertising must refrain from unwarranted nutritional or health claims. The greater part of the book deals with specific types of food, such as fats and oils, fruit juices, canned and dried fruits, etc. This is the type of book to be used primarily for reference. It might well be a part of the kitchen library, and every housewife would benefit

[1] American Medical Association, *Journal*, p. 675, July 3, 1943. For further information concerning the Council on Foods and Nutrition see *Rules and Regulations* of the Council on Foods and Nutrition of the American Medical Association, April, 1942; also *General Decisions on Foods and Food Advertising*, Council on Foods and Nutrition, American Medical Association, April, 1942.

if she did no more than read the introductory statement concerning food products.[1]

The importance of the services of such professional societies as the three mentioned and of others which operate on a less elaborate program is much greater potentially than actually. Their chief advantage is that they are nonprofit, professional organizations whose motives are beyond question. Their chief defect, on the other hand, is their inability to reach consumers. In contrast with the vast audiences available to the commercial advertiser, these societies reach but a few thousands. Nevertheless the importance of the work done by the three associations described can not be measured in the usual way. There can be no doubt that these organizations have exercised and continue to exercise very great influence in the field of consumer welfare.[2]

Are Producer Aids Reliable?

A Qualified Answer. There can be little doubt that the judgments of producers may be biased in their own favor. Indeed it would be strange if the situation were otherwise. Yet this would by no means justify the conclusion that the efforts of some producers to help consumers as described in this chapter are not sincerely conceived and honestly executed. When one considers the fact that there are 184,000 manufacturing firms and 1,770,000 retail stores in the United States, the number of those who are sufficiently concerned with their customers' welfare to make some special effort to assure them of quality and fair price is amazingly small.

Unfortunately, it is difficult for buyers to be sure whether or not they will benefit from such efforts, when made. This skepticism is not without justification. Businessmen keep reminding the public that they are not in business for their health nor are they operating charitable institutions. Taking them at their own word, consumers are justified in concluding that any apparent consumer-aid program will be maintained only as long as it pays measurable profits to the businessman. Consumers have every right to ask who pays for these special services. It takes money to run testing laboratories and to meet the obligations created by guarantees. Business accounting recognizes the validity of charging such costs to operating expenses. Since these firms expect to make what they choose to call a fair profit over and above their expenses of doing business it is evident that those who patronize them pay for the services in

[1] American Medical Association, Council on Foods, *Accepted Foods*, Chicago, 1939.

[2] For further evaluation of this type of producer aid see Bush, George L., *Science Education in Consumer Buying*, chap. 5, "Professional Associations and Related Sources of Consumer Information: a Critical Appraisal," Columbia University, New York, 1941.

the form of higher prices. It may well mean that the higher price thus paid is justified by the greater assurance that the merchandise purchased will prove satisfactory. Consumers might well be excused for believing that since they are paying for such services considerable duplication might be avoided and greater reliability assured if the laboratory testing services were conducted by a nonprofit association owned, operated, and financed by consumers in their own interests. A final answer to the question whether producer helps are reliable is that there is justifiable basis for doubt, stronger in some cases than in others, and that even though their reliability be admitted their number and scope is so limited that they cannot be regarded as an important means of promoting ultimate consumer welfare.

Summary

In their efforts to reassure consumers concerning the superior quality of their products, producers make varied uses of trade-marks, brands, labels, and guarantees. In general the first three of these are of little help to consumers, while the last may be useful in some cases. Testing laboratories can be helpful but are limited in number and scope. Likewise, informational pamphlets can provide consumers with valuable advice, but their number and coverage are small. Customer research is generally a superficial sales device, while the possibility of producers really aiding consumers by providing reliable, useful information in their advertising seems remote. *Good Housekeeping's* Guaranty Seal is difficult to evaluate, but, although it claims the allegiance of thousands of women, its obligation to advertisers cannot be ignored. The joint efforts of producers to win consumer confidence by appearing to aid them are of doubtful value. Although the integrity of professional societies is accepted, their beneficial services reach only a very small number of consumers.

Even though one were to accept these various devices at their face value it cannot be denied that producers are biased in their own favor and that the cost is borne by consumers. That being the case, the consumers may feel with justification that they or their representatives should co-ordinate and control these devices for their benefit.

QUESTIONS FOR DISCUSSION

1. How does the subject matter of this chapter fit in with the theory of monopolistic competition as presented to you in your study of principles of economics?
2. Is the modern use of brands and trade-marks consistent with the theory of pure competition?

3. Does a producer of a branded or trade-marked commodity have a property right in your habit of purchasing his product? Should he have?
4. To what extent have you depended on brands? Trade-marks? Labels? Have you found them helpful?
5. Formerly, a retail merchant purchased a homogeneous product, such as flour, in bulk and he it was to whom the buyer looked for assurance of quality. Today the manufacturer has branded his product, advertised it nationally, and it is an impersonal corporate entity to whom you look for assurance of quality. Which system would you prefer if you could choose?
6. Has your experience with guarantees been satisfactory?
7. Do you deal with a retail firm which maintains a testing laboratory? If so, are you aware of any tangible gain?
8. Does your mother rely on *Good Housekeeping's* Guaranty Seal? Do you? Should you?

PROBLEMS AND PROJECTS

1. Collect several trade-marks and report on their usefulness to you as a consumer.

2. Study the labels on a selected group of products; what helpful information do they provide? What assurance do you have concerning their reliability?

3. Write a report of your family's experience with guarantees.

4. Collect several written guarantees on such items as watches, refrigerators, washers, batteries, and tires, and evaluate them.

5. Secure first-hand information on the testing laboratory of a retail store and present your conclusions as to its benefits to consumers.

6. Interview ten women readers of *Good Housekeeping* and report on their judgment and use of the Guaranty Seal.

7. Summarize the reports of the American Medical Association's Council on Foods and Nutrition in the last three issues of the *Journal.*

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Standards and Grade Labels for Consumers

The Need for Additional Standards

Trade Is Based on Standards. Every commercial exchange involves the use of one or more standards of measure. So accustomed are we to their use that we take for granted such standards as those which measure time, dimensions, bulk, weight, and value. Upon realizing a want for butter one does not go into a store and purchase some butter for some money, but rather asks for a pound for which the price is 51 cents. One does not purchase some eggs for some money, but asks for one dozen which are priced at 60 cents. Neither does one purchase some coal for some money, but specifically requests one ton of bituminous egg size, for ten dollars. One does not purchase some milk for some money, but receives one quart for 16 cents. Nor does one purchase some dress or some suit material for some money; rather one asks for a stated number of yards of a specified material priced at a certain number of cents or dollars.

In all of these cases and in all commercial transactions at least two standards are used. The first of these is a standard of measure or weight. There was a time when weights and measures were not standardized. An ell was a measure of length, the standard for which was the length of the king's arm. This, of course, permitted considerable variation with every change of a monarch. Among the nations of the world there are found today different standards of weight such as the pound, kilogram, and oka. In the United States the National Bureau of Standards and the various state bureaus maintain standards for both weights and measures, the master standards being in the national capital.

The second standard used in all commercial transactions is that for measuring value. In economic language value is the power of one good to command other goods in exchange. Price is a measure of value in terms of money, while money is a universally acceptable medium of exchange, the standard for which in the United States is the dollar, containing 13.71 grains of gold. Although the absolute number of grains of gold in the dollar is fixed, the value of the dollar is relative to the values of all other commodities and services and fluctuates within fairly

wide limits. The value of the dollar is usually expressed as its purchasing power, which is high in some periods and low in others. Many proposals have been advanced for stabilizing the purchasing power of the dollar so that it would function better as a standard of value. Failing adoption of such a plan, the best that can be done with the present monetary standard is to measure changes in its purchasing power by the use of index numbers. This means that we really have two standards—one an unchanging amount of gold, which we call the dollar; the other a fluctuating amount of purchasing power measured by deviations from an index base of 100.

Missing or Defective Standards. Probably the most striking omission in commercial standards is that for quality. A purchaser has little more assurance when he buys a pair of shoes that their wearing qualities will meet his expectations than he would have that he would receive the exact amount of sugar he expected if he asked his grocer for some sugar. By what standard can the purchaser measure the quality of any one of the numerous items which he must purchase regularly in the market? By implication the price which he pays is a measure of quality, but in practice this is no reliable standard. It is not even as desirable as using the king's arm for measuring length, for in this case a high price may mean good quality at one time or in one place while at another time or at another place a low price might secure merchandise of high quality. Considerable evidence demonstrating the unreliability of price as a measure of quality was presented in Chapter 13.

Standards for measuring quality do exist. Either they are not used, or if used they are not usually understood by consumers. Nor do sellers do much to explain the standards they use. In many cases they do more to confuse. Officials of the Columbus (Ohio) Better Business Bureau found themselves confused by local advertising of groceries and meats. They found no way to compare quality and price. So rib roasts were purchased in five different stores, the only statements of quality being general superlatives such as "highest quality always," "better meat at better prices." The five purchases were graded by an official United States government grader with the following results:

Price per Pound	*Government Grade*
$.25	Good
.25	Good
.27	Low Choice
.25	Low Choice
.24	Commercial

These results are not very helpful to the average purchaser, who could scarcely be expected to know that under government grades "Good" is

third grade, "Commercial" is fourth grade, and "Choice" is second grade. The official Federal government standards for beef are Prime, Choice, Good, Commercial, Utility, Cutter, Canner.[1]

When packers of rice describe the various grades by such terms as Extra Fancy, Fancy, Extra Choice, Choice, and Medium, how is a consumer to know that the word Medium indicates rice of fifth-grade quality? In the purchase of brooms one might suppose that the term Fancy Grade indicates highest quality. Actually that term describes second quality, the first quality being covered by the term Super Grade and the third quality by the term Service Grade. French packed mushrooms are described as Extra Miniature, Sur Extra Petite, Sur Extra, Small Extras, Extras, First Choice, Choice, Pieces and Stems. In grading eggs quality measurements are not identical in all markets. In New York the best eggs are Specials, second grade are Standards, while the word First describes a third-grade product. In Chicago highest-quality eggs are described as Extra First, while Firsts are second in grade and Current Receipts are the volume grade. There are, however, well-recognized quality grades for eggs established by state or Federal law. In New York the four grades are Fancy, A, B, and C, while in Illinois the four letters A, B, C, and D are used. These latter are terms which buyers can understand but which they have little opportunity to use. Unfortunately the Federal Department of Agriculture has adopted the terms Specials, Extra, Standard, and Trade. Certainly the ultimate egg buyer has no way of knowing that Extra is second grade any more than that Special is first grade.

When a housewife purchases asparagus both the quality and the amount she receives are almost a matter of chance. In California, Extra Fancy asparagus tips are supposedly first grade, containing from 43 to 67 stalks per bunch. In New Jersey, the same grade contains 30 or fewer stalks to the bunch. The Federal Department of Agriculture has prepared standard grades by number which are available to any grower or shipper but which are used rarely. Under this standard United States No. 1 must contain fresh stalks, well trimmed, undamaged, not less than $\frac{8}{16}$ of an inch in diameter, and they must be fairly straight with the green color covering not less than two thirds of the stalk.

A study of 10,500 labels on various canned goods indicated that there is "no standardized, clear-cut term to indicate the quality." Understandable terms such as Grade A, Grade B, Grade C, Fancy, Choice, or Standard appeared on only 10 per cent or less of the labels except in the case of corn, for which 18 per cent of the labels carried some such term. Since Federal law requires that all labels indicate the net

[1] Columbus Better Business Bureau, *Bulletin*, July 9, 1940.

weight of contents, every one of the labels complied with that provision, yet 97 per cent of them made no indication of the volume of content or of the number of servings or of the number of pieces. Among the fruit labels 85 per cent carried no statement showing the sirup density. On the other hand, 80 per cent of the labels carried pictures of the food in the raw state.

A canning association official reports a study of 474 labels used by 53 firms in thirteen states. For the most part the labels cover the fancy brands, omitting the second and third grades. It was found that 254 different phrases were used to express the size of the peas in the cans. This was quite independent of any quality guides, which were scarcely used except in the form of superlatives usually registered as trade names.

A survey of terms used in designating the qualities of goods, conducted by the Consumers Advisory Board, concludes (1) "that most systems are extremely complicated and decidedly irrational." (2) Grade designations are used much more extensively in the wholesale than in the retail trade. Generally speaking, quality designations disappear just before merchandise passes over the retail counter, leaving the ultimate buyer, whose ability to judge quality is not to be compared with that of the expert wholesale dealer, without any reliable guide. (3) All too frequently there are concealed top grades. To the uninitiated retail buyer the phrase Number 1 would mean the top grade. Actually in the case of potatoes Number 1 is second grade, while it indicates third grade for cheese. Number 2, which should indicate second grade, is used in both cases to designate a product of fourth-grade quality. Top grade for potatoes is designated by the term Fancy, while Extra Fancy indicates top grade cheese. In a study of grading terms one half of those tabulated contained similar concealing top grades. (4) Most grade names consist of superlatives designed to mislead the retail buyer into believing that the products are one or more grades higher in quality than they are actually. Illustrations of this device have been presented in the description of grading terminology for rice, beef, mushrooms, and brooms. As an additional illustration asparagus is graded by the terms Colossal, Jumbo, Extra Select, Select, Extra Fancy, and Fancy. Certainly no buyer would ever suspect that the word Fancy designated a product of sixth-grade quality. In the study to which reference has been made not one case was discovered in which a term indicating understatement of quality was used.

In lieu of clear-cut, definite standards and terms which consumers can understand, American producers have substituted branded and trade-marked names. There is a curious belief on the part of businessmen that the use of a term which indicates clearly that one product is lower

in quality than another is certain to be a serious deterrent to sales. That this is not true has been demonstrated in a number of cases where quality rating in simple language has been inaugurated. Thus the citizens of Oregon have consumed more rather than less butter under the law which requires quality grading. Those manufacturers and packers whose products meet or exceed existing standards are missing a remarkable sales opportunity by failing to publicize the fact. There can be no question that only those whose quality is below an acceptable standard have anything to fear or to lose. The fact that those producing high-quality merchandise have not undertaken a sales campaign featuring quality grades indicates to what extent businessmen are bound by custom. Perhaps they are even more tightly bound by pressure from their competitors operating through their trade associations. There are many ways by which competitors can chastise a too-smart young sales manager whose ideas, in their judgment, upset the *status quo* in merchandising too completely or too rapidly.

A second missing standard is one covering the size and content of containers. More progress has been made, however, in eliminating this condition by the simplified practice program carried on by the National Bureau of Standards. At one time there were 200 different sizes of cans in commercial use. The Division of Simplified Practice has succeeded in reducing that number to 27. In Canada only 11 different sizes are used. The most common can sizes are No. 1 Tall, No. 1 Eastern, No. 2, No. 2½, and No. 303. One would scarcely expect to find any great similarity between Numbers 2 and 303, yet at a short distance it is difficult to distinguish the two. Actually No. 303 is so much smaller that it will fit snugly into a No. 2. Four No. 2 cans contain as much food as five of the No. 303 cans. Yet it is not uncommon for retailers to offer for sale No. 303 cans at the same prices as those asked for the No. 2 size, or even at higher prices. In one test three cans of peas were purchased at retail. One No. 2 size cost 15 cents, the second No. 2 can cost 18 cents, while one No. 303 also cost 18 cents. Upon being graded officially in the Bureau of Agricultural Economics, it was found that the contents of all three cans fell within the limits of Grade B. By weighing the food content of each can, and comparing prices, it was found that the 18-cent No. 303 cost 50 per cent more per pound than the peas in the 15-cent No. 2 can.

At one time there were 40 different sizes of jars and classifications used for preserves, and 25 different sizes for jellies. The Bureau has succeeded in reducing the number of sizes commercially used to 9 and 7. At one time there were 75 odd sizes and shapes of hampers. Under those circumstances it was impossible for a buyer to know the actual content.

There was no standard whatever for the term basket or hamper. It might contain whatever the retailer wished to put in, an amount determined usually by his guess as to how he could realize the greatest profit. While the number of hampers has been reduced from 75 to 8 and the meaning of the term basket has been standardized, cardboard cartons and woven mesh bags continue unregulated. The latter type of container has become a very popular means of distributing oranges. State Departments of Weights and Measures have discovered some storekeepers removing spoiled oranges from the bags without replacing them with others.

In recent years increasing varieties of food products have been offered to consumers in package form. The National Bureau of Standards is now attempting to secure some degree of uniformity in the net weight of food packages. That there is need for standardization is illustrated by the fact that prepared baby food can be purchased only in packages containing $4\frac{1}{2}$, $4\frac{3}{4}$, $6\frac{1}{2}$, and $7\frac{1}{2}$ ounces; hot cereals are available in packages containing 12, 14, 16, 20, 22, 24, 26, and 28 ounces; the variety in the net weights of tomato juice containers is even greater, ranging from 13 up to 47 ounces. A consumer who wishes to compare two different brands or two different sizes of the same brand to discover which is the better buy must be very adept at fractions.[1]

As a result of lack of standardization it has been found that in some lines 80 per cent of the business done is confined to 20 per cent of the goods offered for sale. In one extreme case 3,614 styles and colors were required to meet the demands of 10 per cent of the buyers; 70 styles and colors accounted for the remaining 90 per cent of the business.

Certain ones of the customary standards are defective or at least open to question. Should eggs be sold by the dozen as is the common rule, or by the pound? Certainly one dozen large eggs will weigh more than one dozen small eggs, and Michigan now requires that egg sales be based on weight. What other qualities in addition to size and weight should be considered in the purchase of an egg? Age is certainly important, yet in some states "fresh" eggs may not be over 14 days old, while in others they may be 30 days old. "Iowa's Specials" may not be more than 72 hours old when sold to the retailer. To what extent should egg standards take cognizance of variations in the amount of food nutrients?

Should vegetables be sold by the bunch, basket, or pound? It has been shown that a "bunch" of asparagus in California is vastly larger

[1] United States Department of Commerce, National Bureau of Standards, Miscellaneous Publication M165, *Standardization of Packages;* also Letter Circular, LC 726, June 5, 1943; also *Proposed Federal Standard Food Package Bill*, recommended by the National Conference on Weights and Measures.

than a "bunch" in New Jersey. Exactly how many radishes constitute a bunch? How many tomatoes are there in a basket? There is an increasing tendency among the states to require the sale of fruits and vegetables by the pound. Should coal be sold by the long ton or the short ton, or on some other basis such as the number of British Thermal Units of heat it will yield? An investigation revealed that as between two tons of bituminous coal the grade which appeared the more expensive proved actually the most economical if judged on the basis of its BTU content.

Shoe manufacturers accept the standard of $\frac{1}{6}$ of an inch for each half size and the letters A, B, C, for width, but there is no uniformity from one manufacturer to the next. Moreover, there are some 1,500 different styles made from season to season, and each new style requires a new set of patterns.[1] Traditionally, children's clothing has been purchased on the basis of age as a standard, yet for years mothers have known that an age-10 size would not fit a ten-year-old child. A long step toward standardization was made when the United States Bureau of Home Economics sponsored a Works Progress Administration research project which collected and correlated 147,088 body measurements for children, as a result of which it is now possible more nearly to select the correct size of garments for children. A similar project but on a smaller scale was undertaken to secure standardized measurements for women's clothing.

The Nature and Origin of Standards

What Is a Standard? After comparing several different definitions, Professor Coles concludes that "A standard may be defined as a model for a material object or a rule for a course of action established by authority, custom, or general consent by which others of a like nature may be identified, compared, or regulated, or which in itself represents the ideal or the 'one best' for a particular purpose."[2] A less technical definition of standards was presented by Donald Montgomery to the Temporary National Economic Committee in these words: " . . . quality standards are descriptions of the useful characteristics of commodities drawn up and applied in use in such manner that consumers generally will be able to know the relative quality or usefulness of different goods for different purposes."

The Federal government standard for varnish covers the following thirteen characteristics:

[1] Moffett, Carol Willis, "Why the Shoe Pinches," in *Journal of Home Economics*, February, 1942, pp. 13–17.

[2] Coles, Jessie V., *Standardization of Consumers' Goods*, p. 78, The Ronald Press Company, New York, 1932.

"*Appearance.*—Clear and transparent.

Color.—Not darker than a solution of 1 gram of potassium dichromate in 100 milliliters of pure sulphuric acid, specific gravity 1.84.

Flash point (closed cup).—Not below 30° C. (86° F.).

Nonvolatile matter.—Not less than 55 per cent by weight.

Set to touch.—In not less than 30 minutes and not more than 2 hours.

Dry hard and tough.—In not more than 8 hours.

Viscosity at 25° C.—Not less than 0.85 nor more than 2.00 poises (between C and H on the Gardner-Holdt scale).

Working properties.—Varnish shall have good brushing, flowing, covering, and leveling properties. The dried film shall have the characteristic gloss of spar varnish.

Safety of working.—Shall pass the draft and gas tests.

Water resistance.—Dried film shall withstand cold water for 72 hours and boiling water for 60 minutes without whitening or dulling.

Toughness.—Shall pass a 100-per cent kauri reduction test at 24° C. (75° F.).

Skinning.—Shall be negligible when received, and after 48 hours in a tightly closed half-filled container.

Odor.—The odor in the can during drying and/or after drying shall be not abnormally offensive or disagreeable."

Butter is graded on the following five points: flavor, body or texture, color, salt, and package. Expert graders score the samples, the highest score being 93. Under the state law of Oregon the following scores are translated in increasing letters which are readily understandable.

Score	*Grade*
93	AA
92	A
90–91	B
89–90	C

In much the same way the Federal standard for cheese is based on flavor, color, body and texture, finish and appearance. These typical scores translated into four understandable grades for American Cheddar are as follows:

Score 92, 93, or 94 means US Fancy.
Score 89, 90, or 91 means US No. 1.
Score 86, 87, or 88 means US No. 2.
Score 83, 84, or 85 means US No. 3.

There are laws setting up standards for eggs in twenty states. In ten of them the acts are compulsory. New York and Michigan use the terms Fancy, A, B, and C, grading being based on size and quality.

The time-honored recipe of pound for pound of fruit and sugar forms the basis for the Food and Drug Administration standard for jams and preserves. Products containing 45 or more pounds of fruit to each 55 pounds of sugar constitute Standard, acceptable jams and preserves, while those containing less than 45 but more than 25 pounds of fruit to each 55 pounds of sugar must be labeled as Imitation. Moreover, the labels must show just how the product is an imitation and must specify the amount of added fruit acid and artificial color.

The Federal standard for sheets requires that the material shall be made of thoroughly cleaned cotton free from waste. Every sheet must be free of avoidable imperfections and of defects or blemishes which affect appearance or serviceability. There must be at least 74 threads per inch in the warp and 66 in the filler, with a minimum of 4.6 ounces per square yard. Hems must be 2 inches long at each end or 1 inch at one end and 3 inches at the other. There shall be no less than 14 stitches to the inch, while the breaking strength must be 70 pounds in the warp and 70 pounds in the filling.

An illustrative size standard is that for men's pajama coats, size C. According to one commercial standard these should be 30½ inches long and measure 50 inches in the chest. The armholes should be 22 inches around and the sleeve bottom 13 inches, while the sleeve length should be 33½ inches and the bottom of the coat should be 50 inches around.

In all these cases, whether the buyer is purchasing butter, cheese, eggs, or sheets and pajamas, the existence of such standards would add definiteness to the transaction. Under a system of standards one would not buy a pound of butter for 51 cents, but rather a pound of butter of the grade desired (Grade A for example) at the specified price. Nor would one buy a suit of pajamas for $2.50, but rather a suit of the size desired, with the assurance that it will fit. But the pajama buyer would still have no measure of quality.

Who Determines the Standards? In those cases where standards do exist they may have their origin in the trade and may derive their authority from custom. It should be repeated that for the most part standards do not apply to the retail trade. They are confined largely to the wholesale trade, being replaced by noninformative trade-marks and labels in the retail trade. Among wholesale dealers in cotton, customary quality grading developed in the trade. The haphazard origin of the standards is indicated by the nine terms which represent various gradations. The first grade is called Middling Fair, while other grades in their order are Strict Good Middling, Good Middling, Strict Middling, Middling, Strict Low Middling, Low Middling, Strict Good Ordinary, and Good Ordinary, Even more chaotic is the condition in the leather

tanning industry, which has defied the efforts of the Bureau of Agricultural Economics and of the Tanners' Council to establish some degree of uniformity. In fact every tanner has his own grading system which he finds conveniently flexible to meet competitive conditions. Among four tanners no two use the same grading system, second grade leather being represented by the letters A and B and by the numbers 1 and 2.

Increasingly the standards are being determined by the trade, under authority of associations. Through such an organization the members of a trade agree upon standards of quality and terms for designating variations. The American Society for Testing Materials has established such grades for asbestos yarns. Size designations have been tabulated and with each size is correlated the nominal yardage per pound and the permissible range of variation. Likewise the minimum asbestos content in percentage is indicated for each grade. It is curious, however, that the five grades are all indicated by some combination of the letter A, the first grade being AAAA, the second AAA, the third AA, the fourth A, and the fifth A-1. Of course those in the trade become accustomed to such terminology, but they might just as well become accustomed to a straight numerical or alphabetical rating. The Broom Institute and the National Standards Council have established three grades for brooms, based on quality of broom corn, handle, twine, and wire. The descriptive terms are Super, Fancy, and Service. The New York Cocoa Exchange has established grades based upon soundness of bean, geographical origin, and price per pound.

The American Standards Association is an outgrowth of the American Engineering Standards Committee. It is composed of 26 national industrial associations, 8 departments of the Federal government, and 11 technical societies. More than 500 organizations are co-operating on its projects which comprise the voluntary formulation of standards.

Probably most standards have been drawn by Federal, state, and municipal governmental departments under authority of law. In the Federal government alone there are 45 agencies which work in one or more branches of the general field of commodity standards. Chief among these is the National Bureau of Standards, established in 1901 to continue the duties formerly exercised by the Office of Standard Weights and Measures. "It is charged with the development, construction, custody, and maintenance of reference and working standards and their intercomparison, improvement, and application in science, engineering, industry, and commerce." In fulfilling these obligations the Bureau technicians draw specifications and conduct tests for governmental purchases, which means that practically the entire field of consumer merchandise is covered in these operations. It is estimated that the

Bureau saves as much as $100,000,000 a year over what would be spent if the various departments were to make their own purchases in the retail market in the usual way. When the Federal government shops for merchandise no attention is paid to commercial advertising, nor are traveling salesmen consulted. Experts in the Bureau draw specifications which are submitted to manufacturers for bids. The lowest bidder is given the contract and as the order is being filled samples are subjected to tests to make sure of their compliance with specifications.

Technicians in the Department of Agriculture have drawn the standards for many agricultural products, including beef, lamb, veal, eggs, poultry, butter, fresh and canned fruits, and vegetables. The United States Public Health Service and the Bureau of Dairy Industry have prepared the standards for milk. Standard grades for distilled spirits have been made by the Federal Alcohol Control Administration. Officials in the Government Printing Office have assisted in preparing standards for paper. The Federal Trade Commission has promulgated standard differences for such products as silk, wool, Merino wool, and numerous other products which are frequently imitated and misrepresented.

Many standards have their origin in the enactment of state laws. Twenty states have adopted standards for eggs and at least two have satisfactory legal standards for butter.

Standards in Use

Standards Legally Required. Among the standards in use under legal requirement are those governing the sale of merchandise by weight, measure, or count which have been enacted by state legislatures. Ten states require quality grading of eggs. Forty states have standardized the pound content of a bushel for fruits, vegetables, and grains. Federal law stipulates that packages containing food and drugs must indicate the net weight content if they enter interstate commerce. The Federal Standard Container Act of 1916, as amended in 1928, sets standards of content for various sizes of containers. The Food and Drug Administration has set standards for meats and meat products, eggs and their products, milk and its products, grain products, fruits and vegetables, sugars, condiments, edible vegetable oils and fats, tea, coffee, cocoa and its products, beverages, vinegar, salt, and baking powder. Under the 1930 amendment the Food and Drug Administration has drawn standards for canned pears, apricots, cherries, peaches, and peas. While this law does not require that labels show variations in quality, it does require that they indicate those cans whose contents are substandard. The Agricultural Marketing Service of the United States Department of

Agriculture has developed 22 standards for canned vegetable products and 18 standards for canned fruits.

Probably the majority of municipalities have enacted ordinances setting standards for milk. The cities of Seattle and Schenectady require that all meats sold over retail counters must be graded and stamped according to standards developed by the Federal Department of Agriculture. In 1935 the legislature of Connecticut enacted a law requiring that packages or containers of potatoes must be marked or labeled with the name of the official Connecticut or United States grade or otherwise with the term "Unclassified" or "Ungraded." For the protection of consumers the law specified that farmers selling from house to house, as well as retailers, must comply with the law. When potato farmers in Pennsylvania discovered that potatoes shipped in from other states were yielding better returns on the market they organized their own cooperative marketing grading service. As a result some growers have been able to increase their receipts per hundredweight by 10 to 30 cents.

The American Standards Association is developing a substantial program of standards for consumer goods. Among those completed are standards for domestic gas ranges, laundry stoves, gas refrigerators, gas water heaters, and safety glass for motor vehicles. Among those more recently completed are standards for electrical refrigerators, bedding, upholstery, hearing aids, bed sheets, and sun glasses.[1] Quality grades for 20 products including milk, butter, cheese, eggs, meat, flour, honey, fruit, vegetables, cotton, silk, wool, rayon, leather, coal, fuel oil, gasoline, radios, kitchenware, and silverware, are explained by Gaer.[2]

Optional Standards; Bureau of Standards Willing-to-Certify Plan. Such other standards as may be in use have been adopted voluntarily. This means that most consumers are unaware of their existence and consequently receive no benefit. How many consumers know that there are commercial standards for men's pajamas, wallpaper, plate-glass mirrors, knit underwear, bag and case goods, wool and part-wool blankets? Even if a few consumers were aware of these standards they might very well be skeptical concerning their reliability in the absence of any formal method of enforcement.

A semiofficial, optional plan for establishing the use of standards has been initiated by the National Bureau of Standards. This is known as the Certification Plan, or "Willing-to-Certify" sources of supply, and consists of the compilation and distribution by the Bureau of lists of

[1] Agnew, P. G. "Consumer Standards on the Way," in *Industrial Standardization*, February, 1940, pp. 43–46.

[2] Gaer, Joseph, *Consumers All*, pp. 184–190, Harcourt, Brace & Company, New York, 1940.

sources of supply of commodities produced according to Federal specifications. The lists contain the names of the firms which have indicated their willingness to certify and to guarantee to the purchasers *upon request*, at the time of placing a contract, that the material supplied by them does actually comply with appropriate Federal specifications. According to recent statistics there are over 1,500 Federal specifications, of which the "Willing-to-Certify" plan has been applied to approximately 900.

The potential possibilities and advantages of this plan have impressed its sponsors. By combining the use of labels, guarantees, and advertising it would be quite possible for a manufacturer to appeal to the buying public on the basis that his products conform to the rigid requirements of Federal specifications. A manufacturer of soap has made use of the following label:

"GUARANTEE

"This Liquid Soap is guaranteed to comply with the United States Government Specification No. 27, for Liquid Soap as adopted by the Federal Specifications Board, on June 20, 1922, when tested by methods shown in circular of the Bureau of Standards No. 124. Copies of specifications and methods of testing will be sent gratis upon application."

Another company "certifies that every sheet fulfills all requirements of United States Government master specification No. 304 for high-count cotton sheets and No. 305 for high-count cotton pillow cases . . . used by the Government as a standard for its own purchases."

The hope has been expressed that some of the benefits derived by those who purchase on contract in large quantities may be passed along to the over-the-counter buyer by means of a widespread application of the labeling plan. It is quite possible that some indirect benefits may accrue to the ultimate consumers, but the probable scale on which these can be realized is very severely restricted. This method of percolating benefits down to consumers leaves them scarcely less helpless than before.

In view of the defects in the certification plan as it relates to retail buyers it may well be asked why does not the Bureau inaugurate a comprehensive plan for divulging the results of its tests? Instead of merely publishing the names of those firms willing to certify *upon request*, why does not the Bureau publish the names of those firms whose products actually meet specification tests? The Bureau itself agrees that "from many points of view it would be highly advantageous to be able to issue a list of 'trade brand' manufactured commodities that comply with

certain designated specifications, or a list of firms which manufacture commodities known to comply." The performance of such functions would make it truly a *National* Bureau of Standards whose services would be beneficial alike for producers and for consumers. As operated at present, the Bureau is helpful almost exclusively to business firms in contrast with ultimate consumers.

The Bureau's response to these inquiries is that "it would seem unwise for the National Bureau of Standards to undertake to hold itself responsible for, and give publicity to, any list of approved or certified trade brand articles or a list of manufacturers of such commodities as have been tested by the Bureau and found to comply with certain designated specifications." There is no indication as to why or to whom "it would seem unwise." Quite clearly "it would seem unwise" from the standpoint of certain producing interests but on the other hand it would seem very wise from the standpoint of consuming interests. Officials emphasize also that the act establishing the Bureau does not grant authority for performing such functions. Neither does Congress provide sufficient funds for such an extended program. It is argued also that such a plan would require a tremendous amount of testing. This is probably true, but is scarcely a reason why it should not be undertaken.

Consumers might very well meet these contentions by letting the Congress know that they wish to extend the authority of their Bureau and that they wish to provide the necessary funds. There is no insurmountable reason why the Bureau could not operate on such a practical scale. There are obstacles, to be sure. But if the *Good Housekeeping* magazine can conduct tests upon which it is claimed hundreds of thousands of housewives depend for their buying information, is it too much to expect that a national public institution could do at least as well? If 100,000 consumers can co-operate to perform such services for themselves on a small scale as they have done in Consumers Union and Consumers' Research, is it too much to expect that 100,000,000 consumers could operate in the same way but on a much larger scale through their National Bureau of Standards? Why could there not be a National Bureau of Standards seal with which manufacturers could label their products, thereby guaranteeing to consumers that they meet Federal specifications? Enforcement could be secured by extending the powers of the Food and Drug Administration and the Federal Trade Commission.

No less an authoritative group than the Committee on Distribution of The Twentieth Century Fund believes "that the Bureau of Standards should make tests of leading products for specific qualities and that the results should be made public." The diverse interests and viewpoints of the Committee are indicated by its composition. The chairman, Mr.

Willard L. Thorp, is Director of Economic Research for Dun & Bradstreet. Other members of the Committee were Stuart Chase, economist; Alvin Dodd, president of the American Management Association; John P. Frey, president of the Metal Trades Department of the American Federation of Labor; Carl L. Hamilton, of the firm Booz, Fry, Allen, and Hamilton; Helen Hall, head of the Henry Street Settlement in New York City; Hector Lazo, executive vice president of the Cooperative Food Distributors of America; Paul H. Nystrom, president of the Limited Price Variety Stores Association; and Robert G. Stewart, formerly a Director of the Standard Oil Company of New Jersey.[1]

The Bureau of Standards says that some of its testing information is now available to consumer groups. The General Schedule of Supplies prepared by the Procurement Division of the Treasury Department and printed by the Government Printing Office, contains information relating to articles purchased for the use of Federal agencies on the basis of their compliance with certain definitely identified Federal specifications. The Schedule shows the unit price paid by the government for each article and its source of supply, so far as the government is concerned, as well as the trade brand under which it is marketed. Moreover, there are frequently brief descriptions of the essential characteristics and grades of the various products.

In June, 1939, Representative Lyle H. Boren (Oklahoma) introduced a bill "to aid consumers by setting up standards of quality based on performance as a guide in the purchase of consumer goods." The bill provided that the Secretary of Commerce, through the National Bureau of Standards, be authorized and directed to establish and to publish standards of quality for consumer goods, with the exception of foods, drugs, cosmetics, and other articles for which Federal standards are now provided by law, when in his judgment such standards are in the public interest. There were to be grade designations by the letters A, B, etc., with A always representing the highest grade. Manufacturers were to be permitted to label their goods so as to show compliance, but the label would be required to carry a guaranty that the article met the requirements of the standards. The bill provided an appropriation of $250,000 to carry out its purposes.

Hearings were held for four days, but the proposal never came to a vote in Congress. Representatives of the National Bureau of Standards supported the bill, as did representatives of various consumer organizations. The latter group, however, objected to centering the work in the Department of Commerce on the ground that that Department was

[1] STEWART, Paul W., and DEWHURST, J. Frederic, *Does Distribution Cost Too Much?* p. 352, The Twentieth Century Fund, New York, 1939.

established to advance the interests of businessmen in contrast to those of consumers.[1]

Quality Standards and Practices Needed

Standards, Labels, and Advertising Beneficial to Consumers. A combination of quality standards plainly and reliably labeled and so advertised to the public would constitute a real producer service. Consumers are subjected to a tremendous amount of advertising and are fairly familiar with labels, but their knowledge of standards is negligible. If American producers really care to make their advertising helpful and their labels meaningful, let them combine the use of standards with these two devices. The inability of consumers to buy wisely under the present system has been iterated and reiterated. Consider the problem of a housewife ready to purchase canned goods. She will find that there are nearly 200 brands of corn alone in a given market.[2] Certainly brand names in such profusion can be of no help to her, but she needs information as to the contents of the cans she buys, for the product is concealed and its quality varies among canners, among localities, and from year to year. Only a part of the evidence available has been presented, showing that price is not a helpful guide to quality.

Or suppose a housewife is going to purchase sheets, an item which recurs quite regularly in her budget. In this case she can see and feel the product, yet her inability to choose a good sheet, fairly priced, is indicated in the results of a test of 109 sheets purchased in the open market. Among these sheets there was a range in weight per square yard from 3.27 to 5.26 ounces; a range in tensile strength in the warp from 27 to 68 pounds, in the filling from 21 to 80 pounds; a range in thread count in the warp from 59.6 to 81.5 per inch, and in the filling from 48.8 to 75.3; and a range in sizing from practically none at all to 40 per cent of the total weight of the sheet.[3]

If the labels on canned goods told the housewife not only the brand name but the quality grade together with a representative picture of the contents, the name of the product, the name of the variety or type, the net contents, the name and address of the canner or distributor, with perhaps such supplementary information as where the product was grown, the use to which it is best suited, recipes and the names of other products packed under the same brand, she might then make her purchase with some assurance. Likewise if labels on sheets told her whether they were firsts or seconds, their torn size, their breaking strength, their

[1] See H. R. 6652, 76th Congress, 1st Session, June 5, 1939; *Industrial Standardization*, February, 1940; *Journal of Home Economics*, vol. 32, pp. 170–172.

[2] See page 290.

[3] See also page 252.

thread count per inch each way, their weight per square yard, and the percentage of sizing, she could determine whether the price was satisfactory for a particular grade. Why do not manufacturers, distributors, and retailers provide their customers with such information? What have they to fear if their product is as good as their advertising claims? It is probably true that most manufacturers offer acceptable merchandise. There are many American canners whose products easily meet the requirements of the Canadian quality grading law, yet these canners fail to tell American consumers the distinctions in grade. There may very well be something like a Gresham's Law in the retail market. Instead of quality merchandise driving out the inferior, it is possible that the situation is or may be reversed. Although the number of "chiselers" may be comparatively small, their influence is far-reaching and tends to set the pattern for merchandising. Under these circumstances why do not reputable producers band together in their trade associations and adopt a plan to advertise that their products are marked to indicate quality grade and labeled with guarantees that they meet Federal specifications?

There are, of course, a number of arguments presented in opposition to any simple, understandable plan of labeling. Canners have been urged to adopt the A, B, C systems which would tell the housewife simply and definitely what she might expect to find in the can. Among the objections raised to this proposal it was argued that it is not practical to measure quality so objectively that it will stand a court test in case a consumer contends that the article purchased did not meet the grade specified on the label. It is argued that litigation would result in expensive court cases. Consumers, it is argued, would not buy according to grade but would continue to prefer established, known brand names. It is feared that the volume of advertising would decline and that some of the huge sums already spent to build up good will might be lost since the brand name might lose some of its drawing power. It is suggested that the industry would not abide by government grades. It is feared that consumers, misunderstanding the grading system, would think that any grade below A is undesirable. The quality will deteriorate, it is claimed, since canners will act so as to meet the minimum of each grade. There would be a tendency also for prices to settle at one level for each of the three or more grades. Finally it is contended that the cost of labeling, inspection, and enforcement would place a financial burden on the industry which would be borne ultimately by the final consumers.

As a counterproposal canners have suggested that they adopt a system of descriptive labeling. It is contended that quality cannot be judged objectively. Rather, pertinent information should be placed on the label so that the purchaser may determine for herself whether the

contents of the can possess the qualities she wants. Specific illustrations of the type of labeling they proposed include such terms as "Medium sweet," "Firm, not tough," "Creamy consistency," "Slightly sweet," "Not tender," and "Thin consistency." Their plan would have provided 144 different combinations of such "descriptive" terms for canned, cream-style corn in No. 2 cans. Since corn is packed also in the whole grain and in several other can sizes it is obvious that such a labeling scheme would be cumbersome and ineffective. In fact, it would probably lead to greater rather than less confusion.

Proponents of A, B, C quality grade labeling have answers for all of these objections. To the canners' contention that it is impractical to test quality objectively the reply is that it is being done. For years packers have secured loans from banks and from the Reconstruction Finance Corporation on the basis of warehouse receipts indicating the number of cases of A, B, C grades. Difficulties with grading, it is contended, seem to arise only when the consumer is involved. Practically the only buyers of American canned foods who do not have the opportunity to buy on the basis of quality standards are the ultimate consumers. This point was sharply and succinctly stated in these words:

> "Packs of canned products are graded on quality factors by the packer himself, by the broker, or by the jobber. They are priced by grades. Statistics of the pack are published by grade. Spot holdings are reported by grades. Shipments are reported by grades. Not only is the general trade in canned fruits and vegetables based on grades, but also the vast purchases made by government agencies. Neither the wholesale grocers, nor the food chains, nor the super markets, nor speculators are expected to buy canned fruits and vegetables on descriptive terms alone. Therefore, buying by guess should not be expected of the American homemaker."[1]

Fear of litigation in expensive court cases is dispelled by referring to Canadian experience. During fifteen years of compulsory grade labeling in Canada there were no court tests. Whether or not consumers would buy on the basis of quality grade labeling is, of course, a controversial question. There is no more reason to suppose that consumers would ignore grade letters than that they would base their purchases upon them. In fact, it is probably true that the real fear is that consumers would base their purchases on grade labels. Experience in Canada tends to refute the contention that brand names would lose their good-will

[1] Williams, Paul, Senior Marketing Specialist, United States Department of Agriculture, in a speech before the Better Business Bureau Executives, National Association of Better Business Bureaus, Inc., Los Angeles, California, June 25, 1941, as reported in Research Bulletin No. 1382, January 19, 1942.

value. On the contrary, advertising campaigns are built around quality labels and efforts made to sell larger quantities of those grades which exceed the minimum requirements. To contend that the industry would not abide by the grades seems to be a harsh self-condemnation by canners. Even those outside the industry would be willing to depend upon most of the canners, leaving the chiselers to the disciplinary actions of the trade associations. Of course, if such a plan were inaugurated under legal requirement there would be no serious problem concerning enforcement. Again Canadian experience indicates that neither quality nor price for different grades tends to fall to the minimum. There are variations both in quality and price which are indicated and capitalized in advertising. That consumers do not misunderstand the grading system is demonstrated by figures indicating that in Canada their purchases have been 10 per cent for grade A, 50 per cent for grade B, and 40 per cent for grade C. In the United States the Great Atlantic and Pacific Tea Company voluntarily inaugurated a grade-labeling system in 1935. In 1942 that company's sales of canned vegetables were divided among 60,000,000 grade A, 20,600,000 grade B, 98,000,000 grade C. In the same year sales of canned fruits were divided as follows: grade A, 53,000,000; grade B, 28,000,000; grade C, 25,000,000.

The action of one large distributor in voluntarily offering its customers grade labeled merchandise indicates that not all sellers were then or are now opposed to providing their customers with more information. In 1939 the Agricultural Marketing Service of the United States Department of Agriculture started an experiment which has grown steadily in size and in importance. Under the AMS continuous inspection plan it is possible for a canner to have a Federal government inspector continuously in his plant to supervise operations. If the plant is operated according to the standards set up by the Agricultural Marketing Service, the inspector is then authorized to grade the finished product either A, B, or C. The canner is then permitted to use a shield on his label certifying that his product has been graded either A, B, or C by the United States Department of Agriculture. Interest in this plan has grown until it has now passed the experimental stage. During the 1943 season 83 plants owned by 68 companies signed contracts for continuous inspection service. In 1942 some of those companies had set up a trade association to promote the idea of grade labeling among consumers. Under the title United States Inspected Foods Educational Service, the organization bases its advertising copy largely on the fact that its products are labeled so as to indicate the grade. Described as an X-ray label, the Association copy emphasizes the fact that the grade designation really gives the buyer a look inside the can.

Those who have gone in for continuous inspection service and voluntary grade labeling have found that it pays and are enthusiastic about it. The cost is very small. A Michigan association of cherry growers reported that for two years the AMS inspection service had cost $\frac{1}{4}$ of 1 cent per case of 24 #2 size cans and $\frac{35}{100}$ of 1 cent per case of 6 #10 size.

The Agricultural Marketing Service has attempted to study the reaction of consumers to its continuous inspection service and to grade labeling. Although no definite results are available, the studies indicate that 69 per cent of the buyers preferred United States grade labeling in combination with other types of labeling. Of those who have used U. S. grade labeled products, 97 per cent reported that they would purchase them again, the other three per cent being in doubt. The majority of those who purchased grade A products reported that they would buy grade B or grade C products if available; 86 per cent would buy grade B, 80 per cent grade C. It is significant to find that of the customers interviewed only 30 per cent had previously heard of grade-labeled foods. Perhaps still more significant was the report that 95 per cent of the customers interviewed indicated their wish to know more about grade labels.

The accuracy of grade label claims was challenged by the Better Business Bureaus in 1940 and 1941. In 14 Bureau cities located in the East and Middle West 275 items of canned goods were purchased. Upon being tested by the Agricultural Marketing Service it was found that 9.09 per cent were higher than the grade shown on the label, 60.36 per cent were exactly as labeled, while 30.55 per cent fell below the grade claimed on the label. It was reported that most of the items were purchased in co-operative stores or in "a large well known chain store." What was not made clear in the report as published by the Better Business Bureau, however, was that these items were not packed under the continuous inspection service of the Agricultural Marketing Service. The canners packed their products presumably according to AMS standards and themselves labeled them as being grade A, B, or C, but had no certification from the Agricultural Marketing Service to that effect.

Suspecting that some firms were attempting to capitalize on the growing interest in grade labels, the Food and Drug Administration seized some 50 lots of canned goods in 1941. In all cases these were products labeled by the manufacturer as meeting AMS grade A, B, or C standards. The Food and Drug Administration held that unless the product conformed to the grade printed on the label, the packer was guilty of misbranding under the Federal Food, Drug, and Cosmetic Act. Most packers let their cases go by default, but one large eastern chain store elected to go to court. The Agricultural Marketing Service, having

tested the lot seized by the Food and Drug Administration, graded it B, although it was labeled as A. The canner, on the other hand, insisted that he had taken six samples from the shipment and that the Agricultural Marketing Service had graded them as A. Later the chain dropped its case, admitting that the can contents did not measure up to grade A.

The important thing in both of these cases seems to be that without some policing control the percentage of products falling below the grade claimed on the label can be expected to be quite high. So far there have been no indications that products packed under the continuous inspection service of the Agricultural Marketing Service have fallen below the grade certified by the inspector. It may very well be that the future course of development in this country will be a growing proportion of canners voluntarily packing their products under continuous inspection. Consumers also have the assurance that the Food and Drug Administration is constantly on the job to check on the validity of claims printed on food labels.[1]

How Can Consumers Secure Information? Consumers can and will secure the information they have a right to expect if and when they register effective demand. Individual consumers can make their contribution toward achieving quality labeling by insisting that the retailer from whom they purchase carry a stock of goods so labeled. Failing that, they can shift their patronage to an organization which has adopted voluntarily a system of grade labeling for its canned products. Through membership in consumer organizations more concerted and effective representation can be made. It is not likely, however, that any great progress will be made without legislation.

After 30 years of confusion in terminology concerning wool products, practically all responsible persons at all familiar with the situation agreed that the only way to protect all concerned was by legislation. The situation was not unlike that in the canning industry. An official of the National Association of Wool Manufacturers, speaking in behalf of mandatory fiber identification, said "We believe that the consumer has a right to know what he or she is buying. We have ourselves supported

[1] The story of the controversy over mandatory grade labels in war time as a part of price control is related in Chapter 29. The foregoing discussion has been based on the following sources: United States Department of Agriculture, Miscellaneous Publication No. 460, *The A B C of Canned Fruit and Vegetable Labeling*, United States Government Printing Office, Washington, 1941; "Simple as A B C" in *Consumers' Guide*, March 1, 1940; *Food Industries*, May, 1941; *Journal of Home Economics*, vol. 33 (1941) pp. 31–32; *Business Week*, May 15, 1943, p. 94; *Advertising Age*, July 12, 1943; Better Business Bureau of St. Louis, *Bulletin*, May 28, 1941, *Grade Labeling Survey Shows Amazing Degree of Inaccuracy; Business Week*, June 14, 1941, August 16, 1941, and November 22, 1941; *Tide*, July 15, 1943.

labeling regulations, knowing that there was a very substantial amount of misrepresentation in the sales of so-called wool products which contained varying amounts of wool." A bulletin issued by the Consumer-Retailer Council of the National Retail Dry Goods Association said "No one has been able to suggest a sensible reason why consumers should not have this information expressed in simple, understandable, and helpful language. The informative label attached to the merchandise is a means by which this can be done."

Known as the Wool Products Labeling Act of 1939, the new legislation went into effect July 14, 1941. With the exception of carpets, rugs, mats, upholsteries, and articles whose fiber content is insignificant or which do not enter into interstate commerce, the act applies to any product which contains or in any way is represented as containing wool of any description and from any source. A label must be affixed to each wool product, showing the percentage of the total fiber weight of new wool, reprocessed wool, and reused wool. In addition, if more than 5 per cent of any other fiber is contained, that fact must be shown, as well as the percentage of non-fibrous "loading," "filling," or "adulterating" matter. The label must show the name of the manufacturer or of the seller responsible for the statement of fiber content, and it must remain attached to the article until sold to the final consumer. The figures showing percentages of various fibers must be plainly legible. The Federal Trade Commission is charged with enforcement of the act, which is handled through its usual process of complaint, investigation, and cease and desist order. Willful violations are misdemeanors punishable by fine up to $5,000 or one year imprisonment or both.

During the debate on this act, before its passage, one of the arguments used against the proposed legislation was the fear of many firms that when consumers learned that products were anything less than all wool they might not buy them. The response of the National Consumer-Retailer Council was the recommendation that labels carry full information concerning fiber content, size, total weight per square yard, durability, warmth, color fastness, shrinkage, and instructions for care. Labels of that type are permitted to carry the legend "This is the type of information recommended by the National Consumer-Retailer Council, Inc."

That there was a real need for legislation of that type was indicated when the first products appeared on the market under the new regulations. Men's hose which retail store executives had previously assumed contained 50 per cent wool turned out to have a content of only 18 per cent, while that which had presumably contained 25 per cent wool turned up with a label showing only 6 per cent. A pair of hose which had

previously been labeled "100 per cent virgin wool base, lined with cotton" was marked under the new law as 64 per cent cotton, 36 per cent wool.[1]

Proposals for legislation requiring factual informative labeling are receiving increasing consideration among state legislatures. In August, 1943, a law went into effect in Ohio requiring descriptive labeling on bedding: the labels must indicate whether the bedding contains new, reprocessed, or second-hand material. The articles include mattresses, upholstered springs, comforters, bolsters, pads, cushions, pillows, mattress protectors, quilts, and any other upholstered articles to be used for sleeping purposes. False labeling is prohibited and penalties are provided.[2] Mississippi has passed a bill which requires grade labeling of all gasoline, oil, and petroleum in that state.[3] In the state of Wisconsin, the Department of Agriculture checks all labels on food products. "The label is not just a fancy scrap of paper advertising a product, it is there to assist you in buying . . . " according to the Department which makes sure that all labels tell the truth or resorts to court action to see that they do.[4]

Summary

Buyers are accustomed to basing their purchases on accepted standards of weight, measure, and value, but sellers are loath to provide standards of quality. Wholesale trade is based almost wholly on quality standards, but in retail trade standards are replaced by the meaningless confusion of brands and trade-marks. There are some standards used in retail trade and their number is growing, as a result of legal requirements. The National Bureau of Standards' certification plan is a step in the right direction but it is limited in scope and effectiveness. Consumers should insist that Congress extend the Bureau's powers and increase its appropriations so that a positive plan of quality reporting to consumers could be adopted. Businessmen whose products meet Bureau standards are missing a powerful competitive sales advantage by failing

[1] The foregoing discussion on the Wool Products Labeling Act is based on the following sources: The Federal Trade Commission, *Rules and Regulations under the Wool Products Labeling Act of 1939;* Miller, Henry, *Labeling Under the Wool Products Labeling Act*, an address before the Convention of National Retail Dry Goods Association, June 3, 1941, by the Director of Trade Practice Conferences, Federal Trade Commission; Better Business Bureau of Philadelphia, Retail Advertising Letter, *Summary of Wool Products Labeling Act of 1939*, November, 1940; American Wool Council, *The Wool Products Labeling Act*, June 10, 1941; Woolcott, Roger, "Informative Labeling of Wool Products," in *Journal of Home Economics*, vol. 33 (1941), pp. 241–242; *New York Times*, June 27, 1941, "First Wool Labels Startle Retailers."

[2] Better Business Bureau (Columbus), *Bulletin*, August 5, 1943.

[3] *Printer's Ink*, March 20, 1942, p. 5.

[4] *Consumer News Digest*, September 2, 1941.

to indicate that conformity on their labels and advertising it to their customers. Consumers can speed the general use of quality standards by trading with those who use them and insisting that others adopt them.

QUESTIONS FOR DISCUSSION

1. Heretofore, when purchasing shoes, gasoline, clothing, etc., what standard for quality have you used?
2. If all things you buy were marked to indicate their quality grade would you buy any grade other than "C" or "Third"?
3. In buying packaged goods what assurance do you have that the container is full? What experience have you had?
4. Who defines such standards as are in use? Who enforces them? Who should?
5. Draw up a list of all standards now in use in your community. Who determines these standards? Who enforces them? Were you aware of all of them?
6. What do you think of the Bureau of Standards plan for publicizing the names of those producers who are willing to certify that their products conform to Federal specifications? Had you heard of it before?
7. Choose a product which you buy recurrently and indicate the information concerning it which you would like to have; compare this with the information you get.
8. Do you think that if all canned goods were labeled to indicate quality grade, lower grades would drive higher grades out of the market?
9. Is the expense of quality grade labeling prohibitive?

PROBLEMS AND PROJECTS

1. Prepare a list of typical consumers' goods, including foods, clothing, and house furnishings, and indicate, as a result of your shopping experience, what quality standards and guides are available.

2. Present the printed matter on the labels taken from several cans; what missing information should you have?

3. Make a comparison and, if possible, a collection of containers designed to deceive buyers as to volume of contents.

4. Compile a list of legal standards in your city or state.

5. Submit to the class a selected list of firms "willing-to-certify" their products, as printed in Bureau of Standards Letter Circular 256A, and see how many can identify the firms' products.

6. Write to your Congressman and Senators, asking their opinion of the proposal to increase the powers and facilities of the Bureau of Standards for the benefit of consumers.

7. Interview or write to the proper official of several large manufacturing, packing, or distributing corporations, asking why they do not

indicate quality on their labels in understandable terms and so advertise to the public.

8. Write a report on Canadian experience with grade labeling of canned goods.

9. Secure information from the Federal Trade Commission, the Better Business Bureaus, and the American Wool Council, and prepare a report on the Wool Products Labeling Act of 1939.

10. Write to the Agricultural Marketing Service, United States Department of Agriculture, for information concerning its continuous inspection service; summarize your material in a report.

SUGGESTIONS FOR FURTHER READING

The published material on this subject is limited, but there are some valuable mimeographed studies and reports made by the Consumers' Division of the National Emergency Council and the Consumers' Advisory Board. The National Bureau of Standards will supply mimeographed material on its certification plan. Additional mimeographed material is available at the American Standards Association and the American Home Economics Association.

26

Watch Your Weights and Measures

Units of Weight and Measure. The acts of weighing and measuring are repeated many times a day every day in our lives. Individuals are almost constantly weighing, measuring, or counting the things they buy and sell. This is inevitable in an economy where people specialize and consequently exchange the products of their specialization. Indeed it is so inevitable that there is a tendency to regard it as commonplace. Commonplace facts are often taken for granted, but the accuracy of our weighing and measuring devices cannot be taken for granted.

In an exchange economy where practically everything is bought and sold in the market it is necessary to have standards by which to judge quantity, quality, and price. In Chapter 25 it was shown that prevailing standards of quality are quite inadequate. In this chapter our purpose is to examine the standards by which we measure quantity.

The pervasiveness and importance of standards of weights and measures may be illustrated by starting off the day with a typical consumer. Let us suppose that he lives in a city and purchases his breakfast in a restaurant. He buys orange juice by the glass, coffee by the cup, eggs and toast by count, paying for them with coins of standard weight and fineness. In his day's work he uses paper which is measured by the ream, and makes a long-distance telephone call, the price of which is measured by the number of minutes he uses the wires. If it is a cloudy day electric lights are turned on, the electricity being priced on the basis of the number of kilowatt hours used. In the afternoon he takes a taxi to keep an appointment on the other side of the city, paying the driver on the basis of the number of miles traveled. At the conclusion of the conference he sends a telegram which is paid for according to the number of words contained in the message. At the close of business hours he proceeds to a store to purchase for his wife some cloth, which is sold for so much a yard. On the way home he also buys a box of candy for her, which is priced on the basis of weight. Upon arriving home, it being a cold winter night, he goes to the furnace room to replenish the fire with coal, which is measured by the ton. He lights a wood fire in the fireplace, the wood having been purchased on the basis of cord measure, while the matches were purchased on the basis of numerical count.

All through the day our typical consumer's wife has been purchasing food and other items on the basis of weight, measure, and numerical count. But it is not necessary to follow her activities in order to establish the fact that consumers trade and live on the basis of standards of weight and measure.

What are some of the more common standards of weight and measure in use? Land is commonly sold in the United States on the basis of a unit of measure called acre. Various fruits and vegetables are sometimes sold by the barrel or by the bushel, but in most cases the measure has been defined in terms of cubic inches or of pounds. Petroleum and liquids also are often sold by the barrel or drum but the legal unit is defined in terms of gallons. Grapes and other fruits and vegetables are sold in smaller quantities by the basket, which is defined variously in terms of cubic inch content. Cloth and wallpaper are sold by the bolt or roll, each being defined in terms of yards of length. Precious stones are sold by the carat, a special unit of weight. Stove wood is usually sold by the cord, which is defined in terms of a specified number of cubic feet. Eggs are sold by the dozen, but oysters may be sold by the tub. Nails are sold by the keg or the pound, but coal is sold by the ton. Water and gas are measured by the cubic foot, while electricity is measured by the kilowatt hour.

Most of the foregoing units of weight or measure are defined in terms of pounds, feet, inches, or gallons. There are tables of linear, square, cubic, chain, liquid, apothecaries' fluid, dry, circular, and nautical measure. There is no need to reproduce any of these tables in these pages, for they are readily accessible in various sources, a convenient one being an unabridged dictionary.

Weights and Measures in Action. The consumer-buyer's problem of buying wisely goes beyond the matter of defining the units of weight and measure. It is not enough, for example, to know that a bolt of cloth is legally forty yards long and that a roll of wallpaper contains sixteen yards; how is the buyer to know that in purchasing a bolt or a roll he is getting the full amount called for legally? Nor is it enough to know that the ton is defined as two thousand pounds or a cord as containing 128 cubic feet; in purchasing these fuel commodities how is the buyer to know that he actually gets a full ton or a full cord? A gallon is defined as containing 231 cubic inches, while a pound is defined as containing sixteen ounces or seven thousand grains; but what assurance does a consumer-buyer have that he gets five full gallons of gasoline or four full quarts of motor oil or one full pound of butter?

The answers to these questions are numerous and varied. A yardstick or two thumbtacks placed thirty-six inches apart on a counter are commonly used to measure cloth, paper, and other items sold by the yard.

Still the buyer does not *know* that he receives full measure. He has no guarantee that the yardstick is correct or that it is used correctly; he has no assurance that the thumbtacks on the counter are thirty-six inches apart or that the clerk does not slip an inch or so in measuring. Necessarily the buyer *trusts* the seller, depending on him to dispense full weight or measure or count.

Scales are manufactured to measure pounds, but a cord is measured in terms of cubic feet, being defined as eight feet long, four feet high, and four feet wide. Rarely does the buyer have any effective way of knowing whether his cord of wood is really eight by four by four; those measurements in fact depend partly on how closely the wood is packed. Neither has he any effective way of checking on the load of coal delivered to his bin because he has no scale large enough to weigh such a bulky commodity. As a consequence in many jurisdictions sellers of coal are required by law to deliver to the buyer a certificate of weight signed by the operator of the scale.

Containers are manufactured which presumably hold one quart or one gallon. But unless the buyer watches the attendant actually put four quarts of oil into his crankcase what assurance does he have that he did not get less or more than the amount ordered and paid for? How can a retail buyer of gasoline know that the dispensing pump is correct in design and operation? And how can he be sure that it is used correctly?

Counter scales are common in retail stores, but how can a customer know that they are correct in design and operation? From the viewpoint both of the seller and the buyer it is unfortunately true that scales will continue to function although they do not register weights correctly. Rarely does a scale get out of order so completely that it fails to function. What this means is that scales which appear to be registering weights may be no more accurate than a running clock; both may show weight and time accurately or both may be inaccurate. And although the scales may be correct they may be used in such a way as to register inaccurate weights. This may be done inadvertently or deliberately. Still another complication is the widespread use of prepackaged merchandising. Butter, for example, is rarely weighed in the presence of the buyer; the carton carries a printed statement to the effect that it contains one pound net weight, but unless the buyer actually tests that statement by placing the butter on a scale he cannot be sure that he is getting a full sixteen-ounce pound.

Obviously consumer-buyers necessarily place great faith in the merchants with whom they deal, and so have confidence that the weights and measures in use are accurate and correctly used. Fortunately for them most sellers are honest, according to weights and measures officials.

If that were not true the price which they would pay for merchandise never delivered would be even larger than it is. But even though a retail merchant may be honest he may be unknowingly using defective scales or defective measures which may operate to his loss or the loss of his customers. Clearly there is need for some impartial agency to define the various standards to be used in the market, to test the accuracy of the devices used in measuring merchandise, and to supervise their use so that sellers and buyers may have reasonable assurance that they are delivering and receiving the amount specified in their transactions.

Weights and Measures Laws

Federal Laws. As a matter of fact the Constitution of the United States does give Congress the power " . . . to coin money, regulate the value thereof, and of foreign coin, *and fix the standard of weights and measures. . . .* "[1] Yet this is one power which Congress has failed fully to use. The first Federal law concerned with weights and measures was passed in 1799 but it remained ineffective for the following thirty-six years because no legal standards had been adopted. Those familiar with colonial and early American history will recall that the commerce of those times was characterized by the confusing use of the standards of several different European nations. It was not until 1828 that the first really operative weights and measures legislation was passed. Eight years later Congress passed a joint resolution directing the Secretary of the Treasury to deliver to the governor of each state a complete set of weights and measures to be used in the Federal customhouses. The terms of that resolution were not fully completed until 1850. In 1838 the Office of Weights and Measures was established in the Coast Survey. Then nearly thirty years passed with no significant weights and measures legislation. In 1866 Congress sanctioned but did not require the use of the metric system. Then followed another period of twenty-five years in which there was little Congressional legislation dealing with weights and measures. The next important step was the establishment of the National Bureau of Standards, which since 1901 has functioned as a national center for testing and for promoting the use of uniform weights and measures. But the National Bureau of Standards is an advisory body lacking mandatory power.

In 1912 the Standard Apple Barrel Act was passed, being amended in 1915. That act defined the dimensions of a barrel for fruits and vegetables and other dry commodities. It applies to intrastate as well as interstate transactions since it was passed under the authority of Article I, Section 8, of the Constitution which gives Congress the power to fix

[1] Article I, Section 8. Italics supplied.

the standard of weights and measures. The Standard Container Act of 1916 established the capacities for containers and the dimensions for baskets, but that act was passed under the power of Congress to regulate interstate commerce. In 1928 the Standard Container Act of that year specified the capacities of hampers and baskets.

Among other laws containing weights and measures provisions probably the most significant is the Federal Food, Drug, and Cosmetic Act of 1938. That law provides that containers for foods, drugs, and cosmetics must not be made, formed, or filled so as to be misleading. Moreover it requires that all containers must carry labels showing their contents in terms of weight, measure, or numerical count. Omitting details, from the consumer-buyer point of view the foregoing acts practically cover the exercise of Congressional power dealing with weights and measures.[1] This is a striking fact in view of the strong tendency toward centralization of authority in the Federal government in recent years. Although having clear authority to exercise control, Congress has failed to use it, with the result that there has been an unfortunate hiatus between Federal and state weights and measures legislation and enforcement. Proposals to increase the power of the National Bureau of Standards, giving it regulatory control over weights and measures, have been made from time to time, but were not enacted. As recently as 1938 a bill would have re-established the standards provided in the Standard Container Acts of 1916 and 1928 as well as the Standard Barrel Act of 1915, and, in addition, would have established standards for drums, cartons, crates, boxes, and sacks. Another bill sought to establish greater uniformity in state laws relating to the definition of a bushel, as used for various commodities. The National Bureau of Standards has tried to achieve national uniformity in weights and measures legislation by urging the adoption of a model law, but has met with little success.

State Laws. In view of the specific provision in the Constitution giving Congress the power to fix the standard of weights and measures there was at one time some doubt as to the validity of state laws. It is now generally conceded, however, that states may exercise legislative power in the absence of Federal legislation. Even when Federal legislation has been enacted state laws on the same subject have been held by the courts to be valid if they are consistent with the Federal law. Apparently the only condition under which a state or municipal act would be invalid would be where there was clearly a conflict with Federal action.

[1] HERVEY, George W., and HADSELL, Reign S., *Inspection and Control of Weights and Measures in the United States*, pp. 3–10, Consumers' Counsel Series, Publication No. 7, Consumers' Counsel Division, United States Department of Agriculture, United States Government Printing Office, Washington, 1942.

A survey of state legislation in 1938 revealed that supervision of weights and measures is exercised exclusively by the state in 9 states. Responsibility for weights and measures legislation and administration is divided between state and local officials in 29 states. In 6 states it was found that there is no general weights and measures program. These and the following findings are at best approximate because only 25 per cent of the officials to whom the survey questionnaire was sent supplied information concerning their weights and measures laws.

Comparing the legislation in states and municipalities with the model law recommended by the National Conference on Weights and Measures, it is found that the following provisions of the model act are in effect in 75 per cent of the jurisdictions: the director of weights and measures may issue regulations for the enforcement of weights and measures laws, including specifications and tolerances for all weights, measures, and weighing devices; approved weighing and measuring devices must be sealed or stamped so that the public may readily recognize approved equipment; weights and measures officials may condemn and seize equipment which is beyond repair or which a proprietor failed to have repaired.

The model law provides that all commercial weighing and measuring devices must be tested at least twice a year. This clause is in effect in one fourth of the states, one half of the cities, and two thirds of the counties reporting; in most other jurisdictions such inspection is required but once a year. According to the model law, standard weights and measures must be inspected by state officials at least once in two years; this provision was found to be in effect in a majority of states, cities, and counties reporting. More than one half of the states, four fifths of the counties, and nearly all of the cities require, as does the model law, the inspection of new weighing and measuring equipment. The model law requires that standard weights and measures must be proved by state standards at least once in five years; although most of the city and county ordinances include this provision it is found in the laws of only about half the states, the others requiring such comparisons only once in ten years.

Practically all jurisdictions include the model law provision that all packages must be plainly and conspicuously labeled to show their net content. But only half of the states and three fourths of the cities prohibit the sale of any packaged commodity if the container "is so made, formed, or filled, or if it is so wrapped as to mislead the purchaser." Standard loaves of bread must weigh one half pound or one pound or one pound and a half or multiples of one pound, according to the model law, a provision found in only one fourth of the states and one half of the cities

and counties. A similar provision regulating the sale of butter or oleomargarine in fractions or multiples of pound units was reported in one half of the states and in a majority of the city and county jurisdictions. In most instances the regulations for standard containers for milk or cream were in agreement with the model law. Likewise requirements for the weights of coal, charcoal, and coke were found to conform generally with those in the model law, which requires a 2,000-pound ton and duplicate tickets for each load. The model law provision that wood be sold in the standard unit of a cord of 128 cubic feet is in effect in approximately two out of every three jurisdictions, and all but two officials reported that berries and small fruits must be sold by weight or in containers of one quart, one pint, or one-half pint, standard dry measure. The standard barrel for fruits and vegetables as defined in the model law is compulsory in more than two thirds of the jurisdictions.

Less than one half of the jurisdictions imposed fines in conformity with those recommended in the model law. The smallest fine was five dollars for the first conviction and twenty dollars for a subsequent offense, while the heaviest fine for states and counties was $500, although one city provides a fine as high as $1,000. Imprisonment instead of or in addition to fines is provided in most of the jurisdictions. Three out of every four officials replying expressed the belief that the penalties prescribed by the law in their jurisdictions are adequate.[1]

In supplementary responses to the questionnaire, state weights and measures officials emphasized the lack of a comprehensive statute as a primary hindrance to an effective weights and measures program. For example, the director of the Oklahoma State Bureau of Standards wrote: "You may say that the pertinent laws of this State are antiquated and inadequate, and do not furnish a proper basis for effective enforcement. This is due to a lack of interest in the problem and to some opposition."[2] Inadequate appropriations were frequently reported as a hindrance to effective administration of weights and measures legislation. As a result of the inadequate appropriations the directors of several state departments reported insufficient personnel. Also resulting from inadequate appropriations is a general lack of adequate equipment for testing, particularly large-capacity scales, tanks, and meters.

Enforcement of Weights and Measures Laws

Importance of Adequate Enforcement. Even if every state, county, and municipality had the model weights and measures law on its books,

[1] Hervey and Hadsell, *op. cit.*, pp. 41–46. Students who wish to learn more about the weights and measures administrative organization in their own states will find helpful information in pp. 26–40 of that publication.

[2] *Ibid.*, p. 23.

buyers and sellers would be little if any more protected than under the present situation if there were no adequate enforcement program. Unfortunately for retail buyers the laws are inadequate in many cases and inadequately enforced or not enforced at all in many jurisdictions. "The importance to a community of adequate weights and measures supervision can scarcely be overestimated," according to a competent student of the problem.[1] As an obligation of the state he places this function next in importance to that of maintaining the personal safety and health of the people.

In the light of that statement what does the record show? Outside of the enforcement activities of the Food and Drug Administration in enforcing the weights and measures provisions of that act, there is practically no Federal enforcement program. Turning to the states, we have the statement of a state weights and measures official to the effect that twelve of the states have fairly adequate supervision of weights and measures in use; twelve of the states have about half as much supervision as they ought to have; twelve have only a little supervision; and the remaining twelve have practically no supervisory program. Where there is no enforcement activity approximately half of the weighing and measuring devices fail to meet reasonable standard requirements.[2]

In the survey to which reference has been made, 75 per cent of the state officials and half of the city and county officers reported their convictions that their budgets were insufficient properly to administer the laws. The average per capita expenditures were 2.4 cents for states, 4.6 cents for cities, and 4.3 cents for counties. In a majority of jurisdictions enforcement funds are appropriated from general tax revenue, but in ten states, thirty-four cities, and seven counties fees are collected, in spite of the fact that weights and measures experts condemn the fee system. Some jurisdictions with small populations have tried to reduce enforcement costs by employing part-time sealers, but the general view prevails that that practice is unsatisfactory. The survey disclosed very few prosecutions. No jail sentences have been imposed in more than three fourths of all the jurisdictions. When levied, fines were small, totaling less than $117 per jurisdiction for states, $97 for cities, and $75 for counties. At the time of the survey the state of Mississippi had made no provision or appropriation for the enforcement of the state weights and measures legislation. The director of the Department of Markets

[1] Smith, Ralph W., *Weights and Measures Administration*, p. 2, National Bureau of Standards Handbook, H26, United States Government Printing Office, Washington, 1941.

[2] United States Department of Commerce, National Bureau of Standards, National Conference on Weights and Measures, *Report*, p. 25, Miscellaneous Publications, M159, United States Government Printing Office, 1937.

for Maryland expressed the view that the weights and measures law of that state was not intended to cover retail purchasing. In such jurisdictions consumer-buyers were completely without protection.[1]

Evidence of Short Measuring. In the absence of good weights and measures laws and with little or no enforcement in many jurisdictions it is surprising that there is not more short weighing and short measuring than the evidence indicates. This does not suggest that the extent of these practices is negligible but it is a credit to the honesty of most retail merchants. Weights and measures officials insist that 95 per cent of retail sellers are honest or mean to be, so the problem narrows down to a comparatively small percentage, but in terms of absolute numbers it presents a real enforcement problem.

Weights and measures officials responding to the survey questionnaire reported that 92 per cent of the scales tested were approved, 7 per cent were condemned for repair, and 1 per cent were confiscated. Tests of gasoline pumps and retail meters by all inspectors found 80 per cent satisfactory, 11 per cent needing adjustment, and the remainder designated for repair or confiscation.

In supervising the use of weighing and measuring devices state inspectors found short weights or short measures in 20 per cent of their investigations, while city inspectors reported 17 per cent and county inspectors 14 per cent. State officials checking the weights for coal found 15 per cent short-weight whereas city officials reported 8 per cent and county officials 6 per cent. On the other hand, 12 per cent of the city officials and 30 per cent of the county officers reported no cases of short-weights of coal. Short-weights for bread were found in 8 per cent of the city investigations, 7 per cent of the state, and 5 per cent of the county. Here again there was wide variation, for in one city 375 loaves were weighed of which 49 per cent were short-weight but in another case more than 10,300 loaves were weighed, none of which proved to be short in weight.

Packaged merchandise was inspected for weight in all jurisdictions. Although the total number of packages tested was small the results showed 8 per cent short-weight in cities, 7 per cent in counties, and 5 per cent in state investigations. The reporting officers do not think that their data warrant any general conclusions other than the observation that short-weighing or short-measuring is more serious in some jurisdictions than in others.[2]

Some years ago the Federal Trade Commission in the course of one of its investigations made a test check on the extent of short-weighing and short-measuring. Five bulk articles were purchased from 1,691

[1] Hervey and Hadsell, *op. cit.*, pp. 67–75. [2] *Ibid.*, pp. 62–67.

stores, both independent and chain, in four cities of more than 100,000 population. Of the 6,640 items purchased, 48.9 per cent were short-weight, 39.5 per cent were over-weight, and 11.6 per cent were exactly correct. Of the chain store purchases 50.3 per cent were short-weight, compared with 47.8 per cent for independent stores. Chain store over-weight amounted to 34 per cent compared with 43.8 per cent for independents, while correct weights for chains were 15.6 per cent compared with 8.4 per cent for independents. Of the 6,640 purchases, 12 per cent were preweighed; of those, 64 per cent were purchased in chain stores and it was found that 59 per cent of the items were short-weight compared with 65 per cent purchased in independents and co-operative chain stores combined.[1]

In a radio broadcast sponsored by the city department of weights and measures, the city attorney of Houston, Texas, reported that 654 out of 4,067 scales were found to be in such bad condition that they were condemned and their further use prohibited. In addition 1,528 of the scales were found to be recording false weights. "Many hundreds of thousands of loaves of bread being sold in the city of Houston were found to be three to six ounces short-weight per pound loaf." Eleven plants handling butter were short-weighing up to as much as two ounces per pound.[2]

The county sealer for Los Angeles county (California) reported that when he made his first inspection of gasoline dispensing pumps 51 per cent were found to be incorrect, resulting in an average shortage to the buyer of three cents out of every dollar.

A weights and measures inspector for Dallas, Texas, cited a distributor of prepackaged foods whose packages were supposed to weigh five pounds net; inspection revealed an average shortage of four ounces per package, representing a short-weight loss of 2½ cents to every purchaser.

Much of the evidence concerning short-weighing and short-measuring practices is found in the reports of New York state and city officials.[3] This is partly because of their excellent enforcement program but may be due in part also to a larger number of offenses in large cities. Out of

[1] *Ibid.*, pp. 20–21.

[2] Taken from a radio broadcast dated October 9, 1939, sponsored by the City Sealer of Weights and Measures, originating over station WRR, Dallas, Texas.

[3] The following paragraphs are based on a variety of sources, including the following: Department of Public Markets, Weights and Measures, City of New York, *Annual Reports*, 1934, 1936, and 1938; public statements by Alex Pisciotta, formerly Director of the Bureau of Weights and Measures, Department of Markets, City of New York; radio address by Barnett Kanzer, Director, Weights and Measures Bureau, State of New York, February 16, 1940, titled "The Modern Type 'Gyp' Artist."

1,026 bags of flour 856 were found to be short in weight anywhere from ½ to 20 ounces. Prior to 1938 meat-packers charged retail meat stores for the heavy paper wrapping as well as for the meat. An invoice for 100 pounds of meat usually covered 93 pounds of meat and seven pounds of paper. Retailers then added enough to the retail price of meat to cover their loss and passed it on to the consumers. The net result was that meat buyers were paying meat prices for inexpensive paper. One food item for which inspectors are always on the alert is bread. In order to make the bread appear to be as large as a pound loaf it is reported that certain bakers "blow up" the loaf with air.

In the selling of meat and poultry some amazing short-weighing practices have been reported by weights and measures officials. One device was that of butchers who placed a strip of salt pork containing 1¼ pounds of lead shot in every chicken as it was weighed. In wrapping the purchase for the customer it was a simple matter to withdraw the leaded strip so that it might be used for the next purchaser. A bucketful of such salt pork weights was found in the ice box in one meat store. Texas inspectors discovered a poultry dealer using an alemite pressure gun to force bran mash into the crops of dead chickens so as to increase their weight.

The director of the Weights and Measures Bureau of the state of New York is authority for the statement that the modern "gyp" artist buys the most expensive and the best scales, weights, and measures. Seeing these, the modern buyer is disarmed, thinking he is fully protected against deceptive practices. Some of the more clever dealers actually insist upon weights and measures officials inspecting their scales and marking them conspicuously with an official seal. It is then that such dealers begin their artistic manipulations. These include misreading the figures on computing scales, concealing the scale with other objects so that the buyer cannot see the correct weight, reading the scales on the "swing," or announcing a price without indicating a weight. Some of them use heavy wrapping paper in weighing a purchase or have an electric fan placed directly over the scales blowing down to the extent of one, two, or three ounces. One ingenious merchant had a wire attached to a foot pedal so that he could stand on the pedal and pull the scale down as far as he thought it was safe to do so.

The modern-type "gyp" artist is benefited by prevailing variations in state laws relating to the sale of commodities. In New York a bushel of potatoes must weigh 60 pounds, a bushel of onions 57 pounds, a bushel of dried peaches 32 pounds, and a bushel of dried apples 25 pounds. Of course, equal-sized bushels of potatoes, onions, or dried apples do not always weigh the same, due to differences in size, variety, and tightness

of pack. A Maine potato does not weigh as much as an Idaho potato of equal size; a Long Island potato weighs more when freshly dug than it does a few weeks later. Confusing the situation still more is the fact that other states have established other legal weights for the same commodities. A legal bushel of spinach in North Carolina weighs 10 pounds, in Tennessee 30 pounds; a legal bushel of sweet potatoes weighs 54 pounds in New York, 60 pounds in Maryland, and 46 pounds in North Dakota; a legal bushel of onions weighs 57 pounds in New York, 50 pounds in Pennsylvania, Rhode Island, and Wisconsin; a legal bushel of dried peaches weighs 33 pounds in New York but only 24 pounds in the District of Columbia.

Still another way in which the modern "gyp" artist may work is that of slack-filling his containers. One will heap the measure in the form of a cone, another will fill it slightly rounded, while still another will fill it level full. The Department found 35 different sizes and shapes of containers in which 1½ ounces of grated cheese were sold. One container stood 3½ inches high with a diameter of 2½ inches but only about one inch of the box contained cheese, the other 2½ inches being filled with air.

The director of the Bureau of Weights and Measures for New York City reported the practice of some dealers in 1939 of selling 30-cent ham at the rate of 85 cents a pound by means of wrapping it in cellophane packages which were then sold without any weight marking. In the same way 15-cent cow meat was found offered for sale at 85 cents a pound in cellophane packages prepared as cubed steaks; mutton also was being sold in the same way at the rate of $1.20 a pound.

Prepackaging by the grocer injects a new chance for error in weight or measure. Not only is it possible for some packers actually to short-weight their customers but since so few people actually examine the label showing the net weight of the contents, weights and measures officials have found that a new form of competition is that of reducing the net weight content of the package. This is perfectly legal since the net weight is shown on the label but so far as the customer is concerned it amounts to short-weighing.

Indicative of the carelessness of buyers was the practice discovered by New York City officials of selling six-ounce packages of bacon as half-pound packages. Over 100 retailers pleaded guilty to that practice. In an effort to break it up the Department of Public Markets, Weights, and Measures succeeded in getting nine local packers to agree to discontinue packaging bacon in six-ounce lots.

Much short-weighing could be eliminated if packages were standardized. More than 80 per cent of all fruits and vegetables are packed in 8 general sizes but 32 other sizes are used for packing so-called special

packs. Three of the general sizes vary so little in their cubic capacities and in their dimensions as to encourage deception and misrepresentation. The cubic capacities of some of the general and special sizes vary as little as three tenths of one cubic inch, while the diameter or height may vary by as little as one sixteenth of an inch.

The Cost of Inadequate Enforcement. The foregoing evidence of short-weighing and short-measuring practices has been chosen almost at random from the various reports of state and city weights and measures officials. Illustration could be added to illustration so as to create the impression that such practices were the rule rather than the exception. Fortunately, we have the assurance of weights and measures officials that such is not the case. Several efforts have been made to arrive at a monetary estimate of the cost to consumer-buyers of inadequate weights and measures legislation and enforcement. The New York City Department of Public Markets, Weights, and Measures is reported to have estimated a loss of ten cents a day per housewife in that city.[1] For the city of New York such an apparently small loss mounts up to a total of $26,000,000 a year. If that figure is taken as a conservative estimate and multiplied by the 41,000,000 spending units in the United States in 1943 it is found that consumer-buyer losses due to short-weighing and short-measuring might be as great as $1,279,200,000 annually. This is a tremendous tax for consumers to be paying and for which no benefit is received. On a per-family basis it means a tax of 60 cents a week or $31.20 a year, which would be roughly equivalent to a 5 per cent sales tax on food purchases.

A Texas weights and measures official placed the estimate as high as $54 a year net loss for a family of five due to short-weighing and short-measuring. If he is correct the annual national short-weighing and short-measuring bill would be $2,214,000,000.

Whatever the figure may be, it is a needless reduction of family purchasing power. If consumers were alert and if they had good legislation and enforcement the short-weight and short-measure tax could be practically eliminated. This has been done in a few jurisdictions.

What Can Be Accomplished?

Caveat Emptor or Caveat Venditor? The Supreme Court has ruled that "the fact that a false statement may be obviously false to those who are trained and experienced does not change its character, nor take away its power to deceive others less experienced. There is no duty resting upon a citizen to suspect the honesty of those with whom he transacts business.

[1] Littell, Robert, "Weighed—and Found Wanting," in *The Reader's Digest*, March, 1938, pp. 25–27.

Laws are made to protect the trusting as well as the suspicious. The best element of business has long since decided that honesty should govern competitive enterprises, and that the rule of *caveat emptor* should not be relied upon to reward fraud and deception."[1]

The former director of the Bureau of Weights and Measures for the City of New York has expressed the view that the days when the buyer should beware are gone; that every man, woman, and child has a right to deal with a merchant, depending upon his honesty. The modern rule, says he, should be, "let the seller beware."[1]

Good weights and measures protection involves adequate legislation and adequate appropriation for staff and equipment. Having these, the public officials can then check new scales and measuring devices, inspect those in use, and supervise the practices of sellers in using such equipment.

Consumer-buyers in California, the District of Columbia, Indiana, Massachusetts, Michigan, New Jersey, New York, Texas, and Wisconsin have the kind of weights and measures laws and enforcement which those in other states are entitled to have.

In the state of New York there are 202 weights and measures officials divided among the leading cities and counties. New York City alone has 75 full-time weights and measures inspectors, which is more than the combined total of 17 states whose population is three times greater than that of New York City.

With such a large staff it is possible for those in charge to assign individuals to special tasks so as to achieve maximum efficiency. Some of the men spend their time testing new weighing and measuring devices. Periodically every scale in use is tested and if correct is sealed. After the weighing and measuring devices have been tested the next step in adequate enforcement is to see that they are used carefully and honestly. New York City inspectors exercise daily supervision over the sale of bread, butter, cheese, fruits and vegetables, fish, meat, poultry, milk, groceries, coal, ice, laundry services, gasoline, medical supplies, and other essentials. Sample purchases are made in stores about which customers have complained or in which the supervising officer thinks tests should be made.

In many of the states where good weights and measures protection is provided much of the success has been due to the publicity efforts of weights and measures officials. It is their contention that every buyer is a potential weights and measures inspector. If, by radio broadcast, public speeches, public school programs, and other such media, consumer-buyers are made aware of the problem and of their part in

[1] Pisciotta, Alex, *Misleading Advertising*, a paper delivered at the Fourth Annual Convention of the Virginia Weights and Measures Association, September 20, 1939.

helping to solve it much can be accomplished in providing adequate enforcement.

Good Enforcement—Expense or Investment? Weights and measures officials contend that the cost of maintaining adequate supervision should be regarded in terms of savings rather than expense. In one of his annual reports the director of the Bureau of Weights and Measures for Los Angeles County reported a total operating expense of $85,394.04, equivalent to a per capita cost of slightly over 3 cents. During the year the activities of the Bureau saved consumers approximately $1,250,000. Such a return on an investment of $85,000 is good finance and good government. Weights and measures officials estimate that a complete job of enforcement could be done at a cost of about 6 cents per capita compared with the average per capita expenditure of 2.4 cents by states and 4.6 cents by cities. If the annual loss due to short weights and short measures is $1,279,000,000 according to the lowest estimate, adequate enforcement would pay for itself and leave a gain of about $1,250,000,000 for consumers if every jurisdiction spent as much as 6 cents per capita.[1]

What Should Be Done?

Need for Unified Action. From the consumer point of view weights and measures legislation and enforcement in the United States can best be described by the one word "chaotic." It has been shown in the words of one state weights and measures official that the 48 states fall roughly into four groups according to the weights and measures protection afforded consumers. There is not a single jurisdiction in which the interests of consumers are protected as fully as they should be; there are many jurisdictions in which they are not protected at all.

This unfortunate situation arises out of the failure of both Federal and state governments to exercise the constitutional power they possess. So many years have passed without adequate Federal governmental action that it is unlikely that there will ever be full independent exercise of Federal power. On the other hand, the states have had adequate time to enact effective weights and measures legislation but have failed to do so. There is no evidence that such lack of action will be corrected reasonably soon.

The experts who deal with weights and measures have long been keenly aware of the need for uniformity and minimum standards in weights and measures legislation. Soon after the National Bureau of

[1] Department of Markets, New York City, *Annual Report*, 1936, p. 45; 1938, p. 30; 1939, p. 3; 1940. Also National Defense Advisory Commission, Consumer Division, Bulletin No. 9, 1941, *Check Your Weights and Measures*, pp. 4–8; this Bulletin was prepared by the writer while a member of the staff of the Consumer Division in 1940–41.

Standards was established in 1901 a compilation of Federal and state weights and measures laws revealed then, as the recent survey also reveals, a set of antiquated, weak, and contradictory statutes which were not being enforced in many states. The Annual National Conference on Weights and Measures was inaugurated in 1905. Those in attendance recognized the need for uniform legislation, and one outgrowth of the second conference was a resolution instructing the executive committee to draft a model law. The Committee performed its task and presented its results to the Conference in 1911. The recommendations were adopted by the Conference and, with a few subsequent amendments, have been urged by the Conference on the various states. But the number adopting the model legislation is disappointingly small.[1]

Moreover, the preceding evidence indicates that adoption of the model law by every one of the 48 states would do little to remedy the problem of inadequate weights and measures protection unless adequate enforcement machinery and appropriations were provided. In the same year in which the National Conference on Weights and Measures adopted the model law which it recommends, *Printers' Ink* also recommended that the various states adopt a model statute regulating advertising. The latter statute has been enacted in a number of states, but no one familiar with the problem of advertising control would contend that adoption of the model statute by itself accomplished very much in the way of advertising control.

It has been suggested that the solution to the weights and measures problem lies in joint Federal-state action.[2] The pattern of joint action used in securing national social security legislation suggests one possible line of action. Under its constitutional power over weights and measures and over interstate commerce the Federal government might enact legislation providing a national system of weights and measures legislation and enforcement containing a grant-in-aid feature which would make it possible to have reasonably uniform minimum standards of legislation and enforcement. Those states enacting satisfactory legislation, which might well be the model law recommended by the National Conference on Weights and Measures, would receive Federal grants-in-aid for enforcement and administrative purposes, while those states failing to enact such legislation would not receive Federal assistance. This is only a rough suggestion, the details of which might vary, but it indicates a wise course of action. There are several ways in which such a plan might be financed, but it seems to be the judgment of weights and measures officials that the best plan is to provide enforcement funds out

[1] Smith, Ralph W., *Weights and Measures Administration*, pp. 241–243.
[2] Scheurer, William A., in *Scale Journal*, vol. 26, No. 10, p. 8.

of general tax revenues. The total amount need not be very large, and as offset by fines on violators and by savings to consumer-buyers would result in large gains rather than a cost to most people. Probably the strongest feature of this proposal is that it would preserve for the states local administration and enforcement yet at the same time would eliminate those blank areas now dotting the weights and measures legislative map.

Better Business Bureaus representing retail merchandising interests, and consumer organizations representing the consumer-buyers' interests, would do well to join forces to secure some such weights and measures program as this. Clearly this is a problem in which the interests of honest sellers and honest buyers coincide. Both need assurance that the laws under which they operate and the devices which they use are properly defined and supervised.

An Immediate Program for Individual Consumers. If one is to be realistic it must be admitted that the possibility of securing an adequate weights and measures legislative program is remote. This means that consumers must continue to look after their own interests as best they can in those states in which their governments are doing nothing or not enough. In some jurisdictions, unfortunately, the consumer-buyer is almost completely the victim of circumstances over which he has no control and about which he can do nothing. Assuming, however, that there is state legislation of some kind and assuming that provision is made for the testing of new weighing and measuring devices as well as for the infrequent testing of devices in use, the individual buyer who is on the alert can substitute for an enforcement officer if he follows some of the suggestions made by weights and measures officials.

As was indicated in Chapter 17, the intelligent consumer-buyer must do his or her own marketing personally. In following the suggestions made in that chapter it will be recalled that one of the last steps in a wise buying process is that of checking weights and measures. Enforcement officials in several states emphasize the importance of insisting upon making one's purchases on the basis of weight or measure or numerical count. If on the latter basis the buyer should check the count of the salesperson; if on the basis of measure the buyer should check the measuring device to be sure that it has been used properly. For example, if liquid is being purchased the buyer should make certain that the container has been completely filled, and that it has no false bottom or other deceptive devices. If the purchase involves the use of a scale the first thing to do is to look for the inspector's seal indicating that the scale is accurate. Then the buyer should notice whether the scale is resting flatly on the counter, whether it is in balance, and that it starts at zero instead of an

ounce or two over. The buyer should see to it that there is nothing on the scale before his purchase is weighed. If it is a spring type of scale the buyer should insist that the seller allow the item to rest on the scale long enough for the indicator to come to a stop. It is important to be sure that unnecessarily heavy wrapping paper or other such materials are not included in the net weight. If lard is purchased in a paper container the buyer should refuse to buy the paper container at lard prices. If such practices are followed any seller who might otherwise be inclined to resort to short-weighing or short-measuring devices would be much more hesitant than in the case of the customer who pays no attention to the weighing process. Especially is this true if the buyer does not hesitate to call attention to what appear to be inaccuracies. The latter should be called to the seller's attention just as a mistake in making change; in fact, short-weighing and short-measuring are special ways of shortchanging. A final checkup might well be made when the buyer gets his purchases home. A Texas housewife was reported by the Texas Director of Weights and Measures to have saved enough by reweighing her purchases at home to pay for her scale in two months' time.[1]

In purchasing prepackaged merchandise weights and measures officials urge buyers first to look for a plain statement of net weight on the label, then to reweigh the contents to see if they coincide with the label statement, and finally if the package is deceptive in appearance or short-weight in content to report it first to the merchant and then to the state weights and measures official.

In purchasing gasoline motorists are given three specific suggestions by weights and measures officials. First, they should look for the inspector's seal indicating that the dispensing pump is accurate. If it is the calculating type of pump it is important to be sure that the indicator starts at zero; one of the most common short-measuring devices reported by weights and measures officials is that of starting the indicator somewhere to the right of zero. In sparsely settled areas of the country the glass bowl type of dispensing pump is still rather commonly used. At best that was a very uncertain measuring device and the motorist needs to be alert to see that the bowl is completely filled before the operator starts emptying its contents into his tank. Finally, the buyer should compare the total sum demanded by the operator with the price per gallon and the number of gallons claimed to have been delivered. It is recommended that motorists should also get out of their cars and watch the operator as he dispenses the gasoline or motor oil or anti-freeze solution. The Superintendent of Weights and Measures for the District of Columbia reported that in one year a single firm defrauded Washington motorists of approxi-

[1] *Check Your Weights and Measures*, p. 10.

mately $100,000. The general manager of the American Automobile Association reported to the 1929 meeting of the National Conference on Weights and Measures "that the motoring public in the United States is being robbed by dishonest operators of retail gasoline pumps of a sum conservatively estimated at 20 million dollars annually."[1]

A cartoon which attracted wide attention not long ago showed a coal buyer in the darkness of his coal bin patiently weighing each lump of coal on a small set of household spring scales with a maximum capacity of two pounds. The cartoonist emphasized sharply the problem faced by coal buyers. Weights and measures officials receive many complaints of short weights but it is difficult to prove a shortage. State and municipal officials stress the importance of buying coal from a reliable dealer and insisting upon receipt of a signed certificate showing the net weight delivered as well as the grade of the coal. It is important also, they say, to be sure that the tickets have not been altered. In case of any doubt the buyer should report to his weights and measures official.

In order to follow the foregoing rules effectively the individual consumer-buyer should know the law pertaining to weights and measures in his own jurisdiction. For example, coal is sold by the long ton of 2,240 pounds in some jurisdictions, whereas in practically all others a ton is defined as 2,000 pounds. Illustrations have been given showing the disparity in weight per bushel of various commodities among some of the states. For example, the weight of a bushel of sweet potatoes varies from 46 to 60 pounds in different jurisdictions.

It is important also that the foregoing rules be followed intelligently and understandingly. Weights and measures officials insist that on the basis of their experience they are convinced that 95 per cent of all those who sell at retail by weight and measure are honest. This suggests that the careful consumer buyer should watch his weights and measures in a manner not likely to arouse antagonism. It is not necessary to create the impression that the buyer thinks every seller is dishonest; rather it can be done in such a way as to indicate simply that there are chances for error and that the buyer is on the alert to catch any mistakes. In dealing with merchants regularly if it is found that the buyer is equally quick to report errors in favor of himself as well as those against him it is not likely that he will have much cause to complain of short weight or short measure in future transactions.

Finally, in those cases where it is necessary to report improper use of weighing and measuring devices to state officials the consumer-buyer should regard those officers as friends with whom to co-operate as unoffi-

[1] National Conference on Weights and Measures, *Report*, June, 1937, Miscellaneous Publication, M 159, p. 17.

cial assistant inspectors. The author of the standard handbook used by all weights and measures officials stresses the importance of teaching consumers to use correct buying methods, " . . . the cardinal principles of which are to buy by definite quantity and to check the amount received." After listing some of the things which buyers should be taught, the author of the handbook concludes with the suggestion that they be instructed to report all violations to weights and measures officials.[1] If consumer-buyers would do this on an extensive scale it would reduce greatly the per capita cost of administering weights and measures laws.

Summary

Since we live in an exchange economy, the acts of weighing and measuring are repeated many times every day. It is necessary to have units of weight and measure, to have devices for measuring those units, and to have assurance that those devices are correct and are used accurately and honestly. Although having a clear grant of power to fix the standard of weights and measures, Congress has failed to use it. As a result, practically all control of weights and measures legislation and enforcement has been exercised by the states. There is amazing disparity, however, in the adequacy of laws and their enforcement. One fourth of the states have fairly adequate weights and measures supervision; one fourth have about half as much supervision as they should have; one fourth have only a little supervision; and one fourth have practically no supervision of weights and measures. There is much evidence of short-weighing and short-measuring; but the surprising thing is that there is not more. Weights and measures officials insist that 95 per cent of retail sellers are honest or mean to be. On a per family basis the short-weighing and short-measuring "tax" amounts to 60 cents per week or $31.20 a year; this is equivalent roughly to a 5-per-cent sales tax on food purchases. Yet adequate enforcement would cost only 6 cents per capita and would represent a good investment. According to the lowest estimate adequate enforcement would pay for itself and leave a gain of at least $1,250,000,000 annually.

But there is no evidence that either Federal or state governments will soon provide effective legislation and enforcement. This means that consumers must continue to look after their own interests as best they can, intelligently and understandingly so as not to arouse antagonism among honest merchants. This involves checking weights and measures at the time of purchase, and a knowledge of the law pertaining to weights and measures in one's own jurisdiction. Improper use of weighing and measuring devices should be reported to a local or state official.

[1] Smith, Ralph W., *Weights and Measures Administration*, p. 130.

QUESTIONS FOR DISCUSSION

1. How well do you know your tables of measures and weights?
2. Until now how much attention have you given to measure, weight, or count as you carried on your daily consuming activities?
3. Do you read the label statements of net contents on packaged merchandise? Can you depend on them?
4. Is a usable scale accurate?
5. What constitutional authority does Congress have over weights and measures? To what extent has it been exercised?
6. What are the weights and measures provisions of the Federal Food, Drug, and Cosmetic Act of 1938?
7. Do all states have adequate weights and measures legislation and administration?
8. Where there is no enforcement activity what proportion of the weighing and measuring devices meet reasonable standards?
9. What are several methods of short-weighing and short-measuring against which you should be on guard?
10. How much short-weighing and short-measuring "tax" do consumers pay annually?
11. What plan of joint Federal-state action is proposed to secure effective weights and measures legislation and enforcement?

PROBLEMS AND PROJECTS

1. Make a list of the various ways in which you use or depend on standards of weight, measure, or number in a typical day.

2. Prepare similar lists based on the daily activities of your mother and your father.

3. Classify a dozen or a score of items in a grocery store according to the standard of measure, weight, or count on which sales are based; do you have a working knowledge of all these tables on the basis of which you can calculate fractional amounts?

4. During a week when you are home check-weigh all packaged merchandise coming into the house and report your results.

5. Secure a copy of your state laws pertaining to measures and weights and compare them with the model law.

6. Make a study and write a report on weights and measures laws and their administration in your county or city.

7. Compare the legal bushel weights for selected fruits and vegetables in your state with those of two or three other states.

8. Interview your county or city Sealer or a weights and measures inspector and write a report describing his functions.

9. Outline a plan of joint Federal-state weights and measures legislation and administration.

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Governmental Aids to Consumers: Positive

FEDERAL AGENCIES SERVING CONSUMERS

Federal consumer services and agencies are found in nineteen bureaus and divisions located in four departments and seven independent offices. These are in addition to such wartime agencies as the Office of Price Administration, the Office of Civilian Requirements of the War Production Board, the Office of Civilian Defense, and the Office of Economic Stabilization.[1]

In contrast to the chapter which follows, this discussion is concerned with the positive efforts of government to assist consumers. The distinction between positive and regulatory governmental aids is found in the tendency of the latter to restrict the unhampered exploitation of consumers by unscrupulous producers, while the former attempts to help consumers by providing them with positive information. In some cases it is difficult to make a clear distinction. While most of the activities of the Food and Drug Administration are regulatory some of its functions are clearly positive.

In addition to the agencies described in detail in this chapter there are others whose functions are indirectly helpful to consumers. Again it is difficult to distinguish always between the positive sort of consumer service and the regulatory type. Most of the services of the various Federal agencies fall within the regulatory classification and will be included in the following chapter. However, the Bureau of Dairy Industry, although it operates primarily for the benefit of farmers, "developed sanitary methods of handling milk on the farm, in transit, and in various plants. . . . " Obviously, all improvements in the direction of sanitation operate indirectly to the benefit of the ultimate consumer, although that is not the direct purpose for which the Bureau operates. Likewise the Bureau of Animal Industry "conducts scientific investigations of the cause, prevention, and treatment of diseases of parasites of domestic animals. . . . " Although this is done for the benefit of the farmer it

[1] Temporary wartime consumer agencies are discussed in Chapter 29.

operates indirectly for the benefit of the consumer. The Forest Service promotes conservation and the wise use of forest land, relating its program to flood control, irrigation, water power, development and maintenance of wild life, and outdoor recreation. There are also a number of free services, such as the provision of parks, and recreational activities and facilities. In the city of Washington the Smithsonian Institution maintains the United States National Museum, the National Gallery of Art, and the National Collection of Fine Arts.[1]

There are several agencies in the Federal government charged with increasing the quantity and quality of housing units. In 1942 several of these were combined under the National Housing Agency which includes the Home Owners Loan Corporation, the Federal Home Loan Bank System, the Federal Savings and Loan Insurance Corporation, the Federal Housing Administration, and the Federal Public Housing Authority.

The Federal government has gone into the insurance business on a huge scale. Millions of men and women are insured by United States Government Life Insurance or by National Service Life Insurance. More information concerning these services will be found in Chapter 21. The Bureau of Old-Age and Survivors Insurance, operating within the Social Security Board under the Federal Security Agency, administers a plan which provides monthly benefits for insured workers and their wives when they reach age 65 and for their children under 18 years of age. In addition the Bureau of Public Assistance administers provisions for grants for old-age assistance, aid to dependent children, and to the needy blind. This is an illustration also of the overlapping of positive services performed by Federal and state governments, since all forms of assistance must be initiated by the states and administered by them.

The foregoing illustrations are not intended to serve as complete citations of indirect consumer services in the Federal government. They do suggest the extent to which the agencies mentioned and others relate their work or some part of it to consumer welfare.[2]

The following description of consumer services performed in various Federal agencies is arranged alphabetically.

Department of Agriculture. (1) The only major bureau in the entire

[1] Gordon, Leland J., *Directory of Governmental Consumer Services and Agencies*, Office of the Consumer Adviser, The Advisory Commission to the Council of National Defense, Washington, D. C., 1940, p. 19.

[2] A helpful source of information concerning the organization, operation, and services of the various Federal governmental agencies is *United States Government Manual*, Division of Public Inquiries, Office of War Information, Washington, D. C. This may be obtained from the Superintendent of Documents at $1 a copy, or through your Congressman without cost. It is revised three times each year.

Federal government devoted to the interests of consumers is the Bureau of Human Nutrition and Home Economics in the Department of Agriculture, established as the Bureau of Home Economics in 1923. Its activities are numerous and varied. For the purpose of helping American families make the best use of their resources the Bureau carries on research on foods, fibers, and other agricultural products used in day-to-day living. This work includes the planning of diets to safeguard health; assaying food for vitamin content so as to enable and encourage people to secure their vitamins from natural food so far as possible; conducting laboratory experiments to determine the daily quota of different vitamins needed for adult health and for growing children. Other activities include the testing of food values and the cooking qualities of dehydrated foods; the development of new and better ways of cooking food so as to conserve its vitamin, mineral, and other nutritional values; the preparation and recommendation of recipes for low-cost foods to be used in school lunch programs and community feeding projects; the furnishing of directions for preserving food in home kitchens safely. In addition to its activities dealing with food as related to health the Bureau prepares buying guides for clothing and household textiles so as to help the consumer recognize wearing qualities and standards of workmanship; it suggests designs for home-made clothing and ways to reduce waste in the use and care of clothing. The results of this research are made available through bulletins, press releases, radio talks, and exhibits as well as through co-operating agencies, such as the Office of Civilian Defense.[1]

(2) The Food Distribution Administration was established in the Department of Agriculture in December, 1942, and was consolidated into the War Food Administration in April, 1943. This agency combines the work formerly carried on by the Agricultural Marketing Administration, the Bureau of Animal Industry, and the Food Division of the War Production Board. Although the purpose of the reorganization was to facilitate the war effort, most of the services formerly carried on by the absorbed agencies were continued. This is the agency which, with the advice of other war agencies, allocates food to meet major wartime requirements and directs the Office of Price Administration to ration various foods so as to provide equitable distribution of supplies to civilians. It develops nutritional standards for the purpose of allocating foods and promotes food conservation by householders.

Community school lunch programs are a joint undertaking of the local communities and the Food Distribution Administration, the purpose of which is to provide a nutritious noon-day meal for children

[1] *United States Government Manual* (Summer 1943) *op. cit.*, pp. 351–352.

attending public schools below the collegiate level. Local interests sponsor the program, make all the arrangements, and share in the cost of the food purchases.

The school milk program is designed to make milk available to children who need it at a cost of one cent per half pint. Local communities make the necessary arrangements with local dairies for the milk and the Food Distribution Administration reimburses the community.

The Food Distribution Administration conducts a nation-wide market news service as well as inspection and grading services. Consumer market news broadcasts are made regularly over a number of radio stations. The names of those carrying these broadcasts may be secured from the Administration.

Official standards have been formulated for nearly all farm products, including several processed foods, such as meats, butter, eggs, canned fruits and vegetables. Although the use of most of these standards is voluntary, they make it possible to indicate the quality grade on the labels of these products for consumers.

A grading service is available on dairy and poultry products, rice, meat, wool, and canned fruits and vegetables. Food purchased for the armed forces, for families receiving public aid, for free school lunches, and for shipments by the Red Cross are inspected. Meat sold in interstate or foreign commerce or by firms operating under Federal inspection is inspected for freedom from disease and for wholesomeness for human consumption.[1]

As part of the industrial and agricultural recovery programs of 1933, several consumer agencies were established by the executive branch of the government. When the Agricultural Adjustment Act was passed in that year, there was established in the Agricultural Adjustment Administration of the Department of Agriculture a Consumers' Counsel Division to carry out the section of that Act which provided for the consideration of the consumers' viewpoint in its administration. Although the Consumers' Counsel never had independent status and although his functions were never fully accepted by the agencies with which it was necessary to work, the men who held that office gradually established a position for themselves which enabled them to perform valuable service for consumers.

Originally and technically the chief function of that Division was to represent the interests of consumers in all conferences and hearings involving marketing agreements. A second function, and one which was effectively performed, was that of publicizing material relating to mar-

[1] *United States Government Manual* (Summer 1943), *op. cit.*, pp. 333–336.

keting agreements as they affected the cost of agricultural products. The objective was to prevent unnecessary gouging of consumers. Although the original Agricultural Administration Act was invalidated it was followed by the Soil Conservation and Domestic Allotment Act of 1935 and the Agricultural Adjustment Act of 1938. Both of these Acts contained clauses which provided for protecting the interests of consumers and for a time strengthened the position of the Consumers' Counsel. In February, 1940, however, the agency was renamed the Division of the Consumers' Counsel and transferred from the Agricultural Adjustment Administration to the general supervision and direction of the Director of Marketing. With that change the influence and importance of the Division began to wane.

With the inauguration of the national defense program in May, 1940, and the recognition of the need for protecting consumers by the appointment of a Consumer Commissioner on the Advisory Commission for the Council of National Defense, it might have been expected that the Division of the Consumers' Counsel would have been reinforced. Certainly the defense program called for even greater governmental activity in behalf of consumers. But such, unfortunately for consumers, was not the case. Like the Consumer Division of the National Defense Advisory Commission which was absorbed by the Office of Price Administration and made subordinate to its Department of Information, the Division of Consumers' Counsel was discontinued and its information, standards and service functions assigned to other units of the Food Distribution Administration.

Although working under increasing difficulties, the Consumers' Counsel held on to his office until December 31, 1942. Increasing realization of his ineffectiveness came to a head in a sharp disagreement over the method of administering the food rationing program. This led to the resignation of the Counsel, Donald Montgomery, and soon thereafter of several members of his staff.

Probably the most important consumer service rendered by the Division of the Consumers' Counsel was publication of the *Consumers' Guide*, the nature and contents of which are indicated in Chapter 17. This publication is being continued by the War Food Administration with current emphasis, of course, on the war food program. The Division of Consumers' Counsel also conducted a radio broadcast over a National Broadcasting Company hookup under the title *Consumer Time*. This program has been broadcast for over ten years and as of October, 1943, could still be heard over a number of NBC-affiliated stations on Saturdays from 12:15 to 12:30, Eastern War Time. It was continued by the Food Distribution Administration in co-operation with other Federal

agencies working for consumers. The programs gave information on rationing, price control, supplies, conservation, canning, meat grades, household furnishings, canned goods, clothing, sheets, blankets, and many other consumer goods.

Corresponding to the Consumers' Counsel Division of the Agricultural Adjustment Administration in early recovery days was the Consumers' Advisory Board of the National Recovery Administration. Its purposes included representation of consumer interests at code hearings. Upon the invalidation of the National Recovery Act, the Board was reconstituted as the Consumers' Project and transferred to the Department of Labor. Among its objectives were those of stimulating interest in consumer problems, suggesting methods for promoting larger and more economical production of useful goods, facilitating the maintenance and improvement of the American standard of living, and reviewing public policy as it relates to the consumer. Those objectives were sufficiently broad to permit it to undertake practically any specific project. First among those was publication of *The Consumer*, a short-lived venture. Another was that of securing adequate labels and standards for retail merchandise, while a third project was that of examining legislative proposals with a view to securing a hearing for the consumer viewpoint. A final general objective was the development and expansion of County Consumers' Councils whose functions were quite similar to those of the national organization, their duty being to localize those functions within counties.

The Consumers' Project came to an end June 30, 1938, being replaced by the Consumer Standards Project. The new Project was transferred from the Department of Labor to the Consumers' Counsel Division of the Agricultural Adjustment Administration in the Department of Agriculture. There it carried out a program which included the tabulation and analysis of national, state, municipal, and trade standards for consumer goods; tabulation and analysis, in co-operation with the National Consumer-Retailer Council, of a survey of information desired by consumers on merchandise labels; a study of weights and measures laws to ascertain how closely they are supervised; a survey of consumer courses in high schools and colleges; and the assembling and classification of literature pertaining to consumer economics. Always having an uncertain existence and operating on emergency relief funds, the Consumer Standards Project was terminated on June 30, 1941. Research on consumer standards was continued, however, by the Standards Section of the Consumers' Counsel Division which was transferred, upon the dissolution of the Consumers' Counsel Division, to the office of the Deputy Administrator in charge of procurement for

the Food Distribution Administration. There, the Standards Section provides assistance to all branches of the Administration in their procurement activities and in the solution of problems relating to simplification and standards.

(3) The Office of Information is the general clearing house for information concerning the Department of Agriculture. While the main work of the Department and therefore of the Office of Information is concerned with promoting the welfare of farmers, this Office does prepare and issue a syndicate release for radio broadcast which is largely devoted to consumer problems. Bearing the title, *Homemakers' Chats*, the release is issued five days a week to about 300 radio stations. It gives information on war food problems, nutrition, home management and other problems based on data supplied by the various bureaus of the Department. One day each week is usually devoted to answering questions sent in by listeners to programs on which the release is used.

(4) Operating within the Food Production Administration, the Farm Security Administration performs consumer services for farm families by providing loans for rural rehabilitation service. While most of the loans are for productive purposes, in case of urgent need small grants are made for subsistence and medical care. Loans are made to assist in the establishment of co-operative stores or to enable participation in co-operatives already established. More than 117,000 families have been assisted in securing medical and dental care through county-wide associations formed in co-operation with local physicians and dentists.[1]

(5) The Rural Electrification Administration was organized to extend the marketing of electricity in rural areas. Loans are made to finance the wiring of properties in rural areas and for the acquisition and installation of electrical and plumbing appliances and equipment. The latter loans may cover a complete pressure water system for homes and farm buildings.[2]

Department of Commerce. As the name indicates, the Department of Commerce is concerned chiefly with promoting the interests of businessmen. Any benefits which may accrue to consumers are incidental. The work of the National Bureau of Standards has been described in Chapter 25 on Standards for Consumers. The Bureau's certification plan is one activity which may be said to operate indirectly for the benefit of consumers. The evaluation of that plan in Chapter 25 has shown its severe limitations. At the same time its possibilities of working in consumers' interests have been suggested.

[1] *United States Government Manual* (Summer 1943), *op. cit.*, pp. 339–340.
[2] *Ibid.*, p. 363.

Federal Deposit Insurance Corporation. The Federal Deposit Insurance Corporation insures consumer-depositors in 13,347 commercial banks and trust companies. In addition depositors in 53 mutual savings banks were insured by the Corporation. Federal credit unions are consumer co-operative associations organized under the Federal Credit Union Act. The task of administering the credit unions organized under the Act is assigned to the Federal Deposit Insurance Corporation.[1]

Federal Security Agency. The Federal Security Agency was created in 1939. In it are grouped those agencies of the Federal government whose major purposes are to promote social and economic security, educational opportunity, and the health of the citizens of the nation.

(1) The Public Health Service is charged with all matters affecting the protection and improvement of the public health. It engages in research in the causes and methods of prevention and control of disease and the dissemination of health information. In its work the Service co-operates closely with public health authorities in the states and municipalities.

(2) The Food and Drug Administration dates back to 1907 when the Food and Drug Act of 1906 first became effective. The Administration enforces the Food, Drug, and Cosmetic Act of 1938, the Tea Act, the Import Milk Act, the Caustic Poison Act, and the Filled Milk Act. "Its activities are directed mainly toward promoting purity, standard potency, and truthful and informative labeling of the essential commodities covered by the provisions of these five acts." Places of business where foods, drugs, and cosmetics are manufactured or processed are inspected; samples of products entering interstate commerce and coming within its jurisdiction are analyzed to detect adulterated or misbranded articles; in case of detection appropriate action is taken; samples of foods and drugs intended for the armed forces are tested to be sure that they comply with specifications and are otherwise acceptable; upon the request of other governmental agencies food and drug products are tested; standards for foods are formulated and methods of analysis are developed. In all this work the Administration co-operates closely with state and city Food and Drug law enforcement agencies.[2]

As the foregoing concise summary indicates, the chief activities of the Food and Drug Administration are regulatory and will be described more fully in the following chapter. Among the positive services which are indirectly helpful to consumers is that of inspecting the packaging of sea food, upon request. This service is provided at the joint expense of the packer and the Federal government. The packer then is required to

[1] *Ibid.*, p. 475.

[2] *Ibid.*, p. 442.

print conspicuously on his label "Production Supervised by United States Food and Drug Administration." As a result of such inspection service the wholesomeness of canned shrimp, for example, has improved. It is very significant that 92 per cent of the salmon canners voted to reject a proposal for inspection of their packing processes.

Another service to which reference has been made before is that of certifying coal-tar colors. Following a sharp decline in the output of food colors as a result of widespread adulteration, the Administration's plan of certifying the purity of coal-tar food colors was adopted. Today sampling tests are made of the output of practically all firms making such colors. Consumers may be sure of their food colors by purchasing only those which bear a certificate issued by the Food and Drug Administration.

An interesting feature of the Food and Drug Administration's work, but one which because of its very nature receives little publicity, is that of developing new analytical tests for detecting adulterants. An illustration of the type of helpful service being rendered is that of a chemist in the Administration who developed a method for detecting tea-seed oil and distinguishing it from olive oil, which it closely resembles. Increasing importations of tea-seed oil indicated that this substitute was being sold to American consumers as olive oil but it was practically impossible to establish the fraud until a satisfactory method of detection was evolved in the laboratories of the Administration.

Another service which probably benefits many more consumers is that which has resulted in the development of a new fruit wash. For years Administration officials have been struggling with the problem of lead and arsenic spray residue on fruits and vegetables. Heretofore it has been possible to remove the residue only by means of a slow and expensive chemical washing process. Again an expert in the laboratories of the Administration solved the difficult problem by developing a rapid and inexpensive method of removing spray residue. An illustration of differences in motives is recorded in the struggle for a patent to protect this discovery. The Administration's request for a public-service patent was delayed by the contesting claim of a private firm. After several years the court finally issued the patent to the Administration, thereby making its benefits available to all consumers without charge.

(3) Also in the Federal Security Agency, the United States Office of Education is the service and co-ordinating agency for Federal assistance to the nation's schools, colleges, and other educational organizations. It administers the acts for the promotion of vocational education and other functions originally assigned to the Federal Board for Vocational Education, including co-operation with public and private institutions

and the compilation of information and reports to aid local authorities in this work.

In the field of consumer education the Office has sponsored several conferences of consumer educators which have contributed significantly to the crystallization of concepts and the interchange of ideas and experiences so important in the development of a sound educational program. A report of one of these conferences was published under the title *Some Principles of Consumer Education at the Secondary School Level.* Another service of the Office is the preparation and loan through its Information Exchange of packets of materials for teachers and study-group leaders. One series of these packets is devoted to *The Consumer in Wartime.*

For the purpose of co-ordinating the consumer-education programs and activities of Federal agencies with reference to the schools, colleges, and organized adult education groups, the Office has a Committee on Consumer Education and Related Activities. This committee is composed of representatives of the Home Economics, Agricultural, Distributive, Elementary and Secondary Education Divisions of the Office of Education, and maintains co-operative relationships with eighteen branches and divisions of other government agencies. The specific functions of this committee are to co-operate with other government agencies concerned with consumer problems affecting the school program, to plan joint activities involving two or more services or divisions of the Office of Education, and to analyze the functions of the several services and divisions as they relate to consumer education and make recommendations for additional activities as they are needed.

The Office of Education also publishes *Education for Victory* (formerly *School Life*), a bi-weekly periodical which frequently contains articles on consumer problems and consumer education. Some of the consumer subjects covered by articles published in early 1943 are: "Swap Centers for Rubbers," "Economical Use of Fuel," "Important Consumer Problems—1943," "Consumer Emphases in Educational Programs," and "Consumer Education—A Must for Elementary Schools."

Department of the Interior. (1) The National Park Service administers 166 national parks so as to conserve the scenery and the natural and historical objects and wild life in those areas and to provide for the enjoyment of the parks by present and future generations of consumer-citizens.

(2) Although the activities of the Fish and Wildlife Service are beneficial primarily to those engaged in providing commercial supplies of game and fish, some of its activities are indirectly, if not directly, beneficial to consumers. The Service has done much to encourage the

consumption of fish, which is a low-cost desirable food. Among other things the Service administers a Fishery Market News Service.[1]

Department of Labor. (1) Like many other agencies, the Children's Bureau in the Department of Labor is placed in the government department in which it may function most logically. Its responsibilities are described as those of investigating and reporting on the extent to which children are safeguarded in life and health and afforded opportunities for growth and protection. Its field of activity covers "all matters pertaining to the welfare of children and child life among all classes of our people."

(2) The Bureau of Labor Statistics, as its name indicates, is concerned primarily with the interests of workers rather than the interests of the much broader group of consumers. The Bureau's studies of retail prices are of interest to consumers and are available directly. The Bureau has taken official recognition of the co-operative movement also. This has been done through the publication of bulletins giving information as to the proper procedure for the organization and management of certain types of consumer co-operative societies.

Office of the Bituminous Coal Consumers' Counsel. The only Federal agency bearing a consumer name and acting exclusively as a consumer representative to be established by Congressional enactment was the Office of the Bituminous Coal Consumers' Counsel. Originally this was provided in the Bituminous Coal Act of 1937 on the theory, similar to that of the original Agricultural Adjustment Act and the National Industrial Recovery Act, that when producers got together to "stabilize" prices the consumers were entitled to have a representative there to safeguard their interests. His primary job was to see that prices were not raised too much. The Counsel was empowered to offer testimony and argument at these hearings and to examine and cross-examine witnesses and interested parties. He could conduct independent investigations and enjoyed the power of subpoena. Notices of all complaints filed with the Interstate Commerce Commission involving the transportation of coal were given to the Counsel and he was authorized to appear in all such hearings. Neither the Coal Division nor the Consumers' Counsel had authority to regulate retail coal prices. During its operation the Counsel's Office published monthly *Coal Consumers' Digest; Buying and Burning Bituminous Coal, Bituminous Coal Chart,* and *Coal in Your Bin* were published in pamphlet form. Failure of Congress to renew the Bituminous Coal Act in 1943 resulted in its expiration with the consequent demise of the Division and of the Office of Bituminous Coal Consumers' Counsel.[2]

[1] *United States Government Manual, op. cit.*, p. 308.

[2] *United States Government Manual, op. cit.*, p. 533, and correspondence with the Office of Bituminous Coal Consumers' Counsel.

Departmental Publications. Every one of the agencies described in the preceding pages has prepared and published pamphlets describing its work and the results of its research. Some of them publish periodicals. Consumers who wish to make full use of governmental services should secure from each of these agencies or from the Superintendent of Documents a list of publications. They may then order those which are of particular interest. To include a complete list of the publications of all these agencies at this point would extend the chapter unduly, but some of the more significant ones may be mentioned. The Bureau of Human Nutrition and Home Economics has prepared many pamphlets dealing with food and nutrition, textiles and clothing, and household buying. The title of one particularly good pamphlet is *Present Guides to Household Buying*. The Food and Drug Administration *Notices of Judgment* have been referred to in various other connections. Even though the Consumers' Counsel Division no longer continues as a separate agency, *Consumers' Guide* is still published periodically. Its nature and contents are described in Chapter 17. The National Bureau of Standards has published a pamphlet of interest to consumers entitled *Services of the National Bureau of Standards to the Consumer*. Material concerning the certification plan is available upon request. The Children's Bureau has a large number of good pamphlets dealing with child health and care. The Public Health Service has made available a pamphlet telling *What Every Person Should Know about Milk*.

In many cases these published materials are available without charge and in those cases where there is a fee it is merely nominal, usually being five or ten cents per pamphlet.

State and Local Consumer Services

Market Information. For the most part state governmental aids to consumers are regulatory. That is to say, the efforts of state governments to promote consumer welfare have been directed chiefly toward the restriction of certain undesirable commercial practices. This has been done largely by means of legislation rather than by attempting to help consumers to help themselves. In most states it is difficult to find positive consumer services paralleling those rendered by the Federal government. It is true that every state has a Department of Agriculture or its equivalent, but it is true also that these Departments are beneficial almost entirely to farmers as farmers. There may be some grading, but it cannot be very extensive. There is some positive consumer service rendered to housewives in general, but to farm housewives in particular, by state Bureaus of Home Economics or by land-grant and state universities' Departments of Home Economics. There are some notable exceptions.

Alabama, for example, is one of the few states whose Food and Drug enforcement officials publicize the results of laboratory tests by brand name. Citizens of Alabama should be familiar with such publications as Department of Agriculture *Bulletins* 34, 37, and 38.

Connecticut also publicizes the results of its Food and Drug control work. Residents of that state should be familiar with such publications as State Department of Agriculture *Bulletins* 363, 388, and 415. Quite likely later bulletins have been issued revealing the results of laboratory tests on Food and Drug products.

Maine is one of the states which authorizes publication of the results of laboratory tests carried out in connection with Food and Drug control. Typical findings may be found in *Official Inspection* 163, 167, and 171.

Massachusetts has a Division of Markets in Boston which provides consumer market information by radio and other publicity media. The Department of Labor and Industry has a Division on the Necessaries of Life which studies the prices of fuel, gasoline, refined petroleum products, dwelling rents, and other commodities and services which are necessities of life. Massachusetts Consumers' Institute functioned as a WPA educational project comprising five active Institutes in the eastern part of the state. Its activities included daily radio broadcasts of local market information, issuance of monthly bulletins on consumer buying, and supplying speakers on consumer education. The following statement by the Institute reveals the scope of its program:

> "The prime goals of the Massachusetts Consumers' Institute are consumer education, protection, and action. In the consumer educational field we propose to educate consumers to become better buyers, to stretch their dollars more advantageously to themselves in such fields as: food and drug legislation, cooperatives, credit unions, instalment buying, savings bank life insurance, insurance, consumer credit, weights and measures, consumer education in the school curriculum, price-fixing, fabric identification, informative labeling, truthful advertising, medical care, housing, milk hearings, legislation, cosmetics, consumer-retailer relations, consumer bookshelves in all libraries."

The New Hampshire state Department of Health publishes a monthly bulletin under the title *New Hampshire Health News*. This is available without charge and is a helpful source of information for consumers. Of course the articles deal primarily with problems of public health and as such are closely related to consumer welfare. For example, in the issue for May, 1943, one will find the results of analyses of carbonated beverages. A resident of New Hampshire can learn by reading this bulletin how certain branded products purchased in his home town

tested for flavor, solids, bacteria, and colon organisms. Moreover he will learn that some of the flavoring is imitation, that some of the bottles are misbranded or contain considerable sediment or, most commonly of all, contain excessive bacteria.

New Jersey has a Division of Consumer Information in the Department of Agriculture but the indications are that this agency is designed primarily to induce consumers in New Jersey to consume products raised in that state.

North Dakota has good consumer protective legislation. The Regulatory Department enforces the Food and Drug Laws and publishes laboratory test results in bulletins which are available for circulation. Some of the test results are published in mimeographed form which renders them more useful for immediate and general circulation. Results of commodity tests are published, identified by brand name and by the names of the manufacturer and retailer, enabling a resident of Jamestown, North Dakota, for example, to discover that milk supplied by John Doe has 3.5 per cent butterfat, is dirty, and has a bacteria count of 1,158,000 compared with milk sold by Richard Roe which has 4.1 per cent butterfat, a bacteria count of 6,000, and is clean. Comparable information is published for many other food products and for gasoline and oil. Particularly helpful are the published results of laboratory tests on canned goods; for example, a report on tomato catsup indicates the net weight claimed on the label and the net weight actually found, the total solids, ash, salt, acidity, ascorbic acid, specific gravity, the number of insect parts per 200 milligrams, the percentage of mold, and finally the letter grade, either A, B, C, or D. Comparable information is given for each type of food reported. In some cases the prices per pound are given, thereby enabling North Dakota consumers to compare commodities both as to price and as to grade. Information of this type for recent years will be found in *Bulletins* 59, 63, 67, and 68.

Utah through its WPA education program of the State Department of Public Instruction sponsored the Salt Lake Committee on Consumer Problems. That Committee drew on state officials in such departments as Weights and Measures and Agriculture and on other trained persons who pooled their knowledge and published *Consumer Problems Manual* which relates local consumer problems to existing governmental agencies and emphasizes what consumers can do to help themselves.[1]

Weights and Measures officials in California, Indiana, Michigan, New York, and Texas have undertaken educational campaigns designed to tell consumers what is being done and what they can do to secure and

[1] *Directory of Governmental Consumer Services and Agencies*, *op. cit.*, pp. 15–16.

maintain honest weights and measures. In one case the annual reports are written in such a way that they have news value and receive wide publicity. Some officials give talks to schools, parent-teacher associations, service clubs, and other civic organizations in which among other things they advise consumer buyers how to improve their buying practices. Radio programs are provided by Weights and Measures officials in Indiana, New York, and Texas.

Some states have started consumer agencies which have been relatively unimportant or have been discontinued. For example, Michigan established a Consumers' Bureau in the Department of Agriculture in 1938 to supply consumers with proper specifications for any article they might wish to buy, to standardize consumers' goods, to increase the factual content of labels and advertising, and to protect consumers against inferior merchandise and profiteering. The following year the Bureau was discontinued. Minnesota established a Consumers' Division in the Department of Agriculture with power to investigate prices of consumer commodities and services and to publicize production and marketing costs as well as the profits that each manufacturer, producer, dealer, wholesaler, or retailer might make. Although the law is still on the statute books the Division has been abolished and there is no evidence that consumers are receiving the information to which the statute entitles them.

Municipal Consumer Services. Generally speaking, local governmental aids to consumers are chiefly regulatory. These take the form of ordinances which require minimum standards of quality or of conduct on the part of vendors. More attention will be given to these regulations in Chapter 28.

Local market news broadcasts are available to consumers in Boston, Springfield, and Worcester, Massachusetts; in New York City, Cincinnati, Kansas City, Cleveland, Minneapolis, and St. Paul. In most cases these are sponsored jointly by the Food Distribution Administration of the United States Department of Agriculture and state or local Departments of Marketing. The market news broadcasts deal mostly with arrivals of fruits, vegetables, and fishery products but in some cases include price information and suggestions for preparation and use of low-cost items.

Consumers in New York City have the most complete and best organized service of this type. Through the Bureau of Consumers' Service of the Department of Markets, consumers are provided with daily broadcasts on market information. As food supplies pour into the wholesale markets during the early morning hours Bureau inspectors examine quality and then report on prices. At 8:25 A.M. approximately

1,500,000 women listen to a five-minute broadcast of which the following excerpt is typical:

"Good morning, Housewives: . . . June is the month when tomato supplies are heaviest. Already we are receiving liberal shipments from Texas and Florida, which will soon be augmented by the harvest from the truck gardens of Mississippi and South Carolina, and this luscious vegetable is now selling at reasonable levels after a long period of high prices. . . .

"Tomatoes are one of our very best protective foods. They are particularly rich in Vitamin C, which must be supplied daily as it cannot be stored in the body. Tomatoes also contain Vitamin A and B-1, along with iron—the mineral so important for good red blood, and small amounts of other essential minerals.

"The countless ways in which the tomato may be served is another attribute that endears it to menu planners. It is one of our most popular foods for salads. . . . There are all sorts of stuffed tomato salads—some stuffed with cheese, meats, shellfish, celery, or cooked green vegetables—even raw vegetables and usually the tomato pulp is included.

"Likewise tomatoes may be stuffed in many different ways and baked, often being served as the main course of the meal. Sometimes the stuffing is the same as for a salad—or a mixture of well-seasoned bread crumbs and tomato pulp may be used. Broiled tomato halves, with just a bit of salt, pepper, and melted butter on top and put under a flame make an excellent accompaniment for meat and fish dinners.

"The heavy supplies of tomatoes now available should induce the homemaker to put up some for next winter. You know tomatoes are the easiest of all vegetables to can. You don't need any special equipment, even a steam pressure canner. They are largely juice and therefore heat penetrates them quickly. Furthermore, they are an acid food, so all they need for processing is the heat of the boiling water for a reasonable length of time and you will be sure of killing any dangerous or trouble-making bacteria.

"Here is an interesting angle—tomatoes do not lose vitamin C in canning as some other foods do, because the acid in the vegetable protects the vitamins. One other point—canned tomatoes can wait long months on the pantry shelf with only the slightest loss of vitamin C. Other non-acid vegetables are inclined to lose vitamin C gradually as they stand in the can. . . .

"Plentiful supplies of Porgies are available in the wholesale fish market and they continue an excellent 'buy.' Mackerel advanced slightly but is still moderately priced. Other good suggestions include: Haddock, Pollock, Sea Bass, Cut and Buck Shad, Pan Flounders, and small Weakfish."

In addition to these broadcasts the Department conducts cooking schools in the markets. Throughout 1942 eight classes met regularly with a weekly average attendance of about 800. During war emergency conditions and the resulting lack of personnel, these schools were reduced in number.

An illustration of the way in which consumers and producers may be benefited is provided by the Bureau's encouragement of "Fish Tuesdays." As a result of that device producers have found the market for fish stabilized while consumers have secured a wholesome inexpensive food available twice a week.

During the war period the Bureau inaugurated a second daily radio talk which dealt mostly with advice on regulations of the Office of Price Administration, with rationing, and with recipes.

In 1942 inspectors of the New York City Division of Inspection of the Office of the Comptroller rejected 1,605,554 pounds of all types of food. This represented $107,601 worth out of total expenditures of $6,589,398. Bases of rejection are failure to meet specifications concerning quality, size, weight, condition, packaging, or identification. Federal, state, and municipal agencies share in the task of inspecting all food entering the City of New York. Any unwholesome foods are immediately impounded and are released only on the authority of and under the jurisdiction of the City Health Authorities.

Information concerning weights and measures is provided to consumer-buyers in several cities, including Detroit, Terre Haute, and Los Angeles. In Detroit the Weights and Measures Department conducts a long-range educational program designed to reach all children who finish the elementary grades. They are informed of the function of the Weights and Measures Department and told how they can help to stop unfair practices.

Resale Price Maintenance Laws

Price Fixing Becomes Legal. For consumers an ominous turn in state legislation occurred in the 1930's. Sired by the National Industrial Recovery Act and designed to benefit sellers, state price-fixing laws have been passed under the guise of fair-trade laws whose claimed purpose is to protect consumers from merchandise of inferior quality. After years of effort, American consumers had secured the Sherman Antitrust Act, the Clayton Act, and the Federal Trade Commission Act, designed to protect them from monopolistic price fixing. Since the enactment of those laws some American businessmen have attempted to secure their repeal or modification. The National Industrial Recovery Act suspended the antitrust acts so that businessmen might combine in their trade

associations to set minimum prices. A common practice was to base minimum sale price on the cost of production incurred by the most inefficient producer in the industry. That is to say, the codes were used as means of guaranteeing the *status quo* by assuring a profit to every firm in the field. For the more efficient firms this meant excessive profits. Indicative of the trend under the codes is the fact that 125 out of 180 carried clauses prohibiting sales below cost of the most inefficient individual firm. Moreover, 81 codes included open-price systems, 24 limited the hours of machine operation, while several included the basing-point system of pricing which compels consumers to pay freight costs which are never incurred.[1]

Except for section 7(*a*) with its compulsory recognition of collective bargaining, business interests approved the National Industrial Recovery Act with its exemptions from antitrust laws. During the short time the act was in effect, individual firms in many industries laid the groundwork for continuance of monopolistic or semimonopolistic practices. With the invalidation of the act and the return of vigorous competition a new demand was raised, particularly by small business firms, for protection from their large competitors by means of price-fixing laws. Forty-four states,[2] and Congress, have responded with legislation which permits manufacturers of branded or trade-marked goods to enter into contracts with retailers to set the minimum resale prices for their products. Third parties, informed of a resale price, are bound by the contract as fully as though they had joined in the agreement. These acts are usually called "fair-trade" laws and are based on the doctrine accepted by the Supreme Court that a manufacturer may suffer loss of good will as a result of price cutting. It is no mere coincidence that those who have been most persistent in demands for such laws are producers of cosmetics and liquor. Although their apparent purpose is to provide fair competition their net result is to raise prices to ultimate consumers by guaranteeing a liberal, if not excessive, margin to retailers on all trade-marked goods. It is difficult to see how any manufacturer can be prevented legally from setting the ultimate prices for his product under the protection of this type of legislation. In May, 1940, fourteen manufacturers and three trade associations were indicted by a Federal grand jury, charging violation of the Sherman Anti-Trust Act. It was alleged that the defendant had fixed the prices of optical lenses and frames sold in interstate commerce. Holding patent rights, the various firms prescribed the prices

[1] Loucks, W. N., "Price Fixing: The Consumer Faces Monopoly," in *The Annals*, May, 1934, 113–124.

[2] Delaware, Missouri, Texas and Vermont are the four states which do not have resale price maintenance laws.

at which wholesalers could resell the patented article, as well as the price which the retailer must charge the ultimate consumer. It was alleged that 95 per cent of all lenses and frames sold in the United States were covered by the pricing agreement and that a pair of eye-glasses selling for $20 would yield a good profit if sold at $7.50.[1] Even though the court should find these defendants guilty, it would appear that they could accomplish the same purpose by using the state and Federal "fair-trade" laws which legalize price fixing.

In 1942 practically the entire United States wine and liquor industry was charged with having taken advantage of the "fair trade" act of Colorado, passed in 1935. It was alleged that prices had been raised illegally in violation of the Sherman Act. The point at issue is not whether prices may be raised, but rather whether the method by which higher prices have been achieved is illegal. The defendants agreed to plead *nolo contendere* in order that the point of law might quickly be passed upon by a higher court. In the meantime the defendants were fined a substantial sum, but whether those fines will have to be paid awaits the decision of a higher court.[2]

There has been no unanimous demand on the part of manufacturers for "fair-trade" laws. Rather, they have been pushed by a vigorous lobby representing the interests of those who stood to gain.

> "Laws affecting business are usually put on the books by pressure groups. The country's druggists, through the National Association of Retail Druggists, took the lead in the fight for fair trade. Working as a well-oiled lobby, the N.A.R.D. first brought pressure to bear on local legislators to get the various state laws, then plumped for passage of the Tydings-Miller Act, the federal enabling law. Without a rival pressure group the N.A.R.D. found the job comparatively easy."[3]

It is significant that public hearings on proposed price-fixing bills were held in only three out of more than thirty states. A "model" bill as passed by California contained a stenographic error which was reproduced without correction in the laws of ten other states.[4]

[1] *New York Times*, May 29, 1940.

[2] *Business Week*, August 14, 1943.

[3] *Business Week*, July 15, 1939. For additional information as to how these laws were passed, see Walker, Q. Forrest, *The Consumer and the "Fair-Trade" Laws*, R. H. Macy & Co., Inc., New York, 1940; Temporary National Economic Committee, Part 8, *Problems of the Consumer*, pp. 3460–3473; Stewart, Paul W., and Dewhurst, J. Frederic, *Does Distribution Cost Too Much?* pp. 271–277, The Twentieth Century Fund, New York, 1939.

[4] United States House of Representatives, Seventy-fifth Congress, First Session, Report No. 382, *Resale Price Maintenance*.

Although these laws are widespread they have not as yet become generally effective. Most of them pertain to cosmetics, drug preparations, liquors, and books. In those fields their tendency has been to raise prices. In a few months California's "fair trade" act established a 45 per cent profit margin on 1,216 items. In Chicago the Illinois "fair trade" act has resulted in the price increases shown in the following table.

TABLE XL.—PRICES OF COMMODITIES IN CHICAGO DRUGSTORES BEFORE AND AFTER PASSAGE OF ILLINOIS PRICE MAINTENANCE ACT[1]

Items	*Price before the Act*	*Price since the Act*
Shampoo	$0.44	$0.59
Hair tonic	.79	.89
Razor blades	.23	.29
Toothbrushes	.39	.43
Dental cream	.29	.33
Shaving cream	.34	.37
Cough preparations	.49	.49
Foot preparations	.29	.33
Drug items	.64	.66
Face powder	.89	1.10
Salve	1.19	1.19
Eye preparations	.89	.89

A survey of the effects of "fair-trade" laws upon retail prices in a New York department store shows that the prices of cosmetics have been increased 8.5 per cent; of liquors 11.8 per cent; of drugs 16.0 per cent; of books 17.6 per cent; and of miscellaneous items 15.8 per cent.[2]

In Michigan it was found that the minimum legal price for most items was higher under "fair-trade" laws than before. The minimum resale price for 160 drug items was $78.36, which is $18.16 more than the minimum selling price to the public before "fair-trade." Expressed in another way, minimum "fair-trade" prices were found to be approximately 30 per cent higher than before passage of the "fair-trade" act. On the average, prices of Michigan merchandise sold under "fair-trade" rose 15.7 per cent during the same year in which the prices of 81 items not under price control *decreased* 3.3 per cent. A comparison of prices of 43 items sold in Michigan under minimum "fair-trade" agreements and in Kansas City, Missouri, where prices are uncontrolled, shows that Michigan prices were higher than those in Missouri. The 43 items could

[1] *Resale Price Maintenance, op. cit.*, p. 18.
[2] WALKER, Q. Forrest, *The Consumer and the "Fair-Trade" Laws, op. cit.*, p. 26.

have been purchased in Missouri for $34.29 while they would have cost $38.49 in Michigan in March, 1939.[1]

The Druggists' Research Bureau financed a survey to discover and publicize the effects of "fair-trade" on drug prices. The authors of that study found that in the drugstores of forty-two states where "fair-trade" laws were in effect, prices on fifty selected items showed little change; specifically, they found a decline of one per cent from the average pre-"fair-trade" prices. They found that in small towns prices were higher before "fair-trade" and in the larger cities were lower. Yet farther on the report reveals that for 1,490 chain drugstores in forty-two "fair-trade" states the "everyday" price was 2.2 cents higher under "fair-trade" for each dollar quantity at list; the special sale price was 12.3 cents higher for each dollar at list.[2]

Referring to the foregoing survey purporting to show a price decline, Gault says that there is no conflict between his survey and that of the Druggists' because the latter covered only independent druggists who did not cut prices before "fair-trade," while the Michigan study covered stores which had used cut prices.[3]

Referring to the systematic effort of the price-fixing lobbies to make consumers believe that "fair-trade" laws have lowered prices, Walker says, "It ought to be obvious that vested and other interests do not lobby for price-fixing laws for the purpose of lowering retail prices."[4]

Referring to resale price maintenance laws, a corporate official says, "They were not passed for the benefit of consumers. They were passed for the benefit of merchants and manufacturers." He goes on to say that most regulatory legislation passed in the name of consumer protection actually gives somebody "a better chance to mulct the consumer than he would have under fair competition."[5]

Profiteering Conflicts. A business publication condemns legislation of this type as short-sighted, uneconomic, antisocial, and dangerous.[6] Small-business men and consumers have good reason to be fearful of manufacturing and marketing combinations which exercise monopoly

[1] Gault, Edgar H., *Fair Trade*, Michigan Business Studies, vol. IX, No. 2, pp. 29–32, University of Michigan, School of Business Administration, Bureau of Business Research, Ann Arbor, 1939.

[2] Ostlund, H. J., and Vickland, C. R., *Fair Trade and the Retail Drug Store*, pp. 2, 9, 11, 12, 32. Druggists' Research Bureau, Chicago, Illinois, 1940.

[3] Gault, *op. cit.*, p. 37.

[4] Walker, Q. Forrest, *The Consumer and the "Fair-Trade" Laws*, p. 26, R. H. Macy & Co., Inc., New York, 1940.

[5] Scoville, John, Chief Statistician, Chrysler Corporation, Detroit, Michigan. Quoted in Michigan Conference on Consumer Credit, *op. cit.*, p. 107.

[6] Babson's Business Service, *Supplement*, Section Two, vol. 32, No. 15, April 14, 1941.

power. Large-scale manufacturers and marketing combinations, together with consumers, have cause to fear laws designed to guarantee profits to inefficient retailers. Legislation of this latter type is illustrated by the Robinson-Patman Act which among other things forbade manufacturers to grant any greater discount to larger than to smaller customers. Many states have passed anti-chain-store legislation, usually in the form of tax laws, and that passed by the legislature of Louisiana has been held valid by the Supreme Court. There are many other laws of this type aiming at the same general purposes. Their consequence is that consumers definitely lose if they buy, while they lose the use value of goods if they do not buy. The state is now caught in this struggle of economic interests and is expected to subsidize and guarantee profits to all groups. It has become the unhappy mediator between the big-business man and the small-business man. Caught between the upper and the nether millstones, consumers stand to lose regardless of the outcome.

And what will the outcome be? There are several possibilities. Price-fixing legislation might result in more extensive integration of industry. Chain-store marketing units and large department stores may develop their own food-processing or manufacturing activities to a greater degree than at present. At the other end of the process large manufacturers may undertake to set up their own retail outlets.

It is also possible that price-fixing laws may stimulate the use of private brands. Macy's department store, for example, has expanded its line of private "Macy's Own." This product is offered for sale together with a nationally advertised branded product, the latter carrying a tag stating that its price is fixed by the manufacturer while the Macy brand is represented as being as good as or better than the advertised brand.

In 1937 Macy's began to wholesale its private brands to other stores. A subsidiary called Supremacy Products was organized to handle the marketing. Supremacy Products was marketing three thousand Macy items through twenty outlets in 1940, including stores as distant as El Paso, Chattanooga, and Oklahoma City. Macy items are available also at the Food Fair in Baltimore, one of sixty-seven stores operated by Union Premier Stores of Philadelphia.[1]

As a result of this expansion, Macy's is now manufacturing over 650 items in the drug and cosmetic line and has leased additional factory space.[2]

An increasing number of consumers may find escape from price-fixing laws by joining and dealing with consumer co-operatives. The

[1] *Business Week*, February 10, 1940.

[2] *New York Times*, March 7, 1940.

editors of *Business Week* foresaw that danger and warned their businessmen subscribers against it.

> "It is interesting to watch retailers' organizations in the act of stimulating the creation of consumers' co-operatives to compete with retailers. That is what the organizations are unwittingly doing now. They are pushing the Tydings-Miller price resale maintenance bill through Congress and they have induced the legislatures of half of the states to pass similar bills. . . . If all the states passed the price maintenance laws, as they may, a manufacturer will be confronted with a multiplicity of dictation by retailers' organizations in forty-eight states. The consumer will pay—not to outlaw loss leaders and cutthroat competition, but to assure safe profits to even the inefficient retailer. But the consumer will not pay so much indefinitely. The laws that fix retailers' profit margins will be answered with consumers' co-operatives."[1]

What Could Be Done?

A Federal Department for Consumers. In attempting to describe consumer services rendered by various Federal government departments an amazing amount of scatteration has been revealed. Groups of people working more or less for the benefit of consumers are found in four different major departments. The greatest concentration is in the Department of Agriculture, where several different bureaus or other agencies are operated. Because of the extensive and varying activities which may be classified as being in the interests of consumers, a certain amount of diversification is perfectly understandable. The fact that this diversification has attained such proportions is convincing evidence that a Federal Department for Consumers is needed. When the national government was created there was no Department of Commerce, or of Agriculture, or of Labor. As the country grew and as conditions changed farmers organized and demanded active representation in the executive branch of the Federal government. Likewise, businessmen and workers organized and then demanded similar representation. Prior to the establishment of the Departments of Agriculture, Commerce, and Labor, activities beneficial to those various groups were similarly spread out in other departments and their bureaus. Quite clearly the conclusion which may be drawn is that consumers will secure unified, active, and effective representation in the executive branch of their Federal government when they organize and demand it.

A bill to provide for reorganizing governmental agencies and to

[1] *Business Week*, March 13, 1937.

establish a Department of Welfare failed of passage in the third session of the 75th Congress in 1938, after having become a major political issue. The amended proposal would have created a Department of Welfare to promote, together with many other causes, "the protection of the consumer." The Reorganization Act of 1939 did not provide for such a Department, but establishment of the Federal Security Agency as a sub-departmental agency provided an arm through which some of the functions of the proposed Department of Welfare have been performed. The Food and Drug Administration was transferred to this agency, but the Bureau of Human Nutrition and Home Economics remained in the Department of Agriculture.

If and when a Department for Consumers or a Department of Welfare is established it will co-ordinate the scattered consumer activities and unify those not definitely related to the department in which they are found. The work of the Bureau of Human Nutrition and Home Economics, of the Food and Drug Administration, of the National Bureau of Standards, and of the other agencies described in this chapter should be unified in the new Department. The work and results of other agencies of interest to consumers should be co-ordinated. The Food Distribution Administration operates chiefly in the interest of farmers, but some of its work is of interest to consumers and should be made more readily available through an independent department. Another function of the new department would be to assume misplaced duties such as supervision of the Federal Credit Union system.

In addition to unification and co-ordination, consumer activities should be expanded. If 6,000,000 farmers are entitled to a daily radio hour is it too much to expect that over 100,000,000 consumers are entitled to at least as much? The new Department could provide a National Consumer Hour giving out information on the work of the Department pertaining to standards, grading, and tests. If the National Bureau of Standards had just been conducting tests of tooth pastes, the results could be broadcast so that all consumers who cared to follow laboratory tests as a guide rather than advertising claims could do so. In conjunction with the radio the program of consumer publicity should be extended by expanding *Consumers' Guide* into an inclusive weekly magazine. It should be developed as an organ for all consumer news of a more permanent nature than that broadcast by radio. In that respect it would be especially valuable as a medium for reporting the results of laboratory tests or telling what the Food and Drug Administration is doing, and for publicizing standards and quality grades. In his discussion of installment buying, Roger Babson expresses the hope that consumers' organizations will strengthen their position in Washington

Proposed Department for Consumers

Secretary

- **Under-Secretary (Administrative)**
  - Bureau of Publications
    - *Consumers' Guide* (To be a weekly consumers' magazine)
    - Special Bulletins
    - National Radio Hour
  - Legislative Bureau
    (To represent consumers at hearings on all proposed legislation affecting consumers; to publicize desirable and undesirable bills through the Bureau of Publications)
  - Bureau of Research
    (To revive and consolidate the work of Consumer Standards Project and Consumers' Counsel Division; to develop a Division of Consumer Statistics, with emphasis on price data; to study co-operatives; to publicize all findings through the Bureau of Publications)
  - Bureau of Co-ordination
    (To co-ordinate consumer work in other Departments:
    Bureau of Labor Statistics,
    Office of Education,
    Federal Trade Commission
    Rural Electrification Administration
    Federal Deposit Insurance Corporation)
  - Bureau of Public Housing
    (To administer Federal low-cost housing legislation)
- **Under-Secretary (Technical)**
  - Bureau of Consumer Welfare
    (To consolidate and assume the functions of:
    Bureau of Human Nutrition and Home Economics,
    Children's Bureau,
    Public Health Service)
  - Commodities Bureau
    (To replace the Food and Drug Administration; to inspect foods, drugs, and cosmetics and regulate their advertising)
  - Bureau of Standards
    (To publicize tests and specifications through the Bureau of Publications; to issue a *Consumers' Handbook*)

so that the lobbies of other interests will be offset by those of consumers. "The job of keeping clamps on instalment contracting would be an excellent project for a Federal Department for the Consumer."[1]

The chart on page 594 illustrates, in tentative outline, the important services which such a Department could render. To the possible objection that this proposal would expand Federal bureaucracy the answer is clear that for the most part the proposed Department would be consolidating and assuming the work of existing bureaus. The gains for consumers would be much greater representation and efficiency in their behalf at less cost. Under such a plan consumers of all states would enjoy some of the benefits now reserved for consumers in North Dakota. In 1939 the American Association of University Women urged President F. D. Roosevelt to establish a consumer agency as a separate entity or as a bureau in some department "where it could be thoroughly representative of the consumer interests." Again in 1940 a delegation representing sixteen national organizations of women met with Mrs. F. D. Roosevelt and urged establishment of a consumer agency. At that time a preliminary draft of suggestions for such an agency was presented.

State and Municipal Consumer Departments. As in the Federal government, farmers, businessmen, and workers have organized and secured representation in the executive departments of state governments. Within their states and municipalities consumers should insist upon similar representation. These new departments operating to the benefit of consumers could co-ordinate their activities with those of the Federal Department for Consumers, thus providing a complete coverage on consumer information. These state and local consumer departments or divisions could operate in the consumer interest in the following six general ways:

(1) Market information could be made available by radio and bulletins on food, on tests pertaining to local merchandise, on state standards and their use, on the costs of installment buying, and on the sources of small loans. The departments might even inaugurate a small-loan service or at least advise unwary borrowers in their dealings with loan sharks.

(2) They could represent their constituents at hearings pertaining to tax legislation. Experts could present the arguments against sales and excise taxes.

(3) They could represent consumers at budget hearings. Representatives could encourage expenditures for the promotion of general welfare and oppose subsidies for favored groups.

[1] BABSON, Roger, *The Folly of Instalment Buying*, p. 121, J. B. Lippincott Company, Philadelphia, 1938.

(4) The departments could maintain a consumers' lobby to represent the interests of their constituents at hearings pertaining to proposed legislation. It is safe to say that in no one of the 44 states in which price-fixing laws have been legalized have the interests of consumers been represented or considered prior to the passage of such laws.

(5) They could render educational service on the general subject of insurance, with particular emphasis on life, health, accident, and casualty insurance. A series of informative talks and articles could be prepared on the types and functions of insurance, the factual material being obtained from the insurance department.

(6) They could represent the consumer interest in determining educational policy, looking especially toward a shift in emphasis and an expansion in the content of public school curricula so as to provide more effective training in the art of consuming wisely.[1]

Although an encouraging picture can be drawn depicting the possibilities of constructive governmental aids, the impersonality of modern life, coupled with consumer ignorance in the face of fraud and misrepresentation, renders positive aids alone insufficient. Consumers, through their governmental agencies, have found it necessary to declare by legislative laws that producers shall or shall not produce certain commodities in specified ways. In order to enforce these laws constant vigilance on the part of trained experts is necessary. The following chapter is devoted to a discussion of governmental consumer aids of a regulatory type.

Summary

Of the four major departments, with their several bureaus, and the independent Federal offices whose work is affected with a consumer interest, only one Bureau, that of Human Nutrition and Home Economics, is concerned wholly with work beneficial to consumers. State and local governments have quite largely failed to provide positive aid to consumers. The situation demands that the scattered work of Federal agencies be consolidated in a Department for Consumers and that the work of that Department be supplemented by state and municipal consumer departments. The establishment of such a Department in the Federal government would entail little, if any, additional expense, while it would provide consumers with more effective representation looking toward positive improvement of their welfare.

[1] For more details concerning proposed state consumer departments consult, "Proposed State Department: Consumer," published as Chapter XVIII in vol. VIII, *Problems Relating to Executive Administration and Powers*, New York State Constitutional Convention Committee, 1938.

QUESTIONS FOR DISCUSSION

1. Draw up parallel lists of helpful services performed by the Federal government for consumers and for producers. To what conclusions do your results lead? Are you satisfied with present practices and emphases?
2. What do you think are proper functions of the Federal government? Is helping consumers one of them?
3. In 1938 the Roosevelt administration sponsored a Federal government reorganization proposal. If you had been in Congress would you have voted for or against it? Why? Of what interest to consumers was the plan?
4. Is the theory valid that only those who pay taxes are entitled to helpful governmental services?
5. What is the incidence of Federal taxes? Of state taxes? Do your conclusions confirm or invalidate the belief that businessmen support the government?
6. Is there a "fair-trade" act in your state? If so, who secured its passage? Were public hearings held?
7. How does legislation of the "fair-trade" type fit in with the idea of *laissez-faire* and a free, competitive market?
8. Is it a proper state function to legislate on "fair-trade" practices?
9. As a consumer what do you think of "fair-trade" laws?
10. Do you think "fair-trade" acts will speed the growth of consumers' co-operatives?
11. Do you favor in principle the plan of a Department for Consumers?

PROBLEMS AND PROJECTS

1. Secure information from the Federal Bureau of Human Nutrition and Home Economics concerning its work, and present a report to the class.

2. Present all the arguments which come to your mind for and against establishment of a Federal Department for Consumers; secure the opinion of your Representative and Senators on this proposal.

3. Study the proposed organization of the Department for Consumers carefully. What criticisms do you have to offer? What additions or changes would you suggest?

4. Present a critical report to the class on the work of New York City's Bureau of Consumers' Service. (Write to the Bureau of Consumers' Service, Department of Public Markets, Weights, and Measures, New York City, for information concerning its work.)

5. What constructive consumer aids are provided by your state and city governments? Base your report on first-hand information.

6. Secure the opinions of several of your state legislators on the proposal for a state consumer department to operate along the lines suggested on pages 595–596.

7. Write to the North Dakota Regulatory Department, Bismarck, for information concerning state consumer services; summarize the material as a report.

8. If you live in one of the 44 states which have enacted price-maintenance laws secure a copy of the act and present a summary of its significant provisions.

9. If there is a price-maintenance law in your state, try to learn (*a*) what business interests sponsored it; (*b*) what groups, if any, opposed it actively; (*c*) what public hearings, if any, were held.

10. If your state legislature has enacted a price-maintenance law, what effects has it had on the retail prices of merchandise covered by the act?

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Governmental Aids to Consumers: Regulatory Legislation

Protecting Consumers by Law

The Background of Sumptuary Legislation. Judging by the history of sumptuary laws in England, freedom of choice in consumption as enjoyed by modern consumers is a comparatively recent development. In the past, legislators regulated the individual life of the consumer in almost every respect. Authoritarian decrees stipulated the types and amount of food which might be consumed, the number of courses in a meal, the quality and amount of liquor which might be drunk, the clothing which might be worn, and the number of guests who might be entertained. As an illustration, a proclamation by Henry VIII in 1517 decreed that the number of dishes which might be served at a dinner should be regulated by the rank of the highest-ranking diner. If the guest of highest rank was a cardinal, nine courses might be served, while six were allowed for a lord, and only three for a citizen with an income of 500 pounds a year. Seven years earlier, a law had been passed denying to all but the king and his immediate family the right to wear any cloth of gold or purple color. The reason assigned was that attempts of some people to live up to the courtly standard had caused them "to robbe and to do extortion and other unlawful dedes to mayntene thereby their costly arrey."[1]

The purposes motivating these types of laws varied. They included a desire to preserve class distinctions and to check wasteful, extravagant consumption. It is stated that the very earliest English laws of this nature were passed in 1221 and that it was their purpose "to protect the consumer against possible greed and dishonesty of the producer." Prices of commodities were fixed, with penalties for violation, including personal punishment such as the ducking chair or confinement in a pillory. It is reported that these laws were seldom enforced. The evidence indicates that many such laws were added to the statute books and then forgotten.

[1] Baldwin, Frances Elizabeth, *Sumptuary Legislation and Personal Regulation in England*, pp. 9, 141, Johns Hopkins University Studies, No. XLIV, Baltimore, 1926.

For example, a regulatory law passed in 1336, during the reign of Edward III, was not repealed until the reign of Queen Victoria.[1]

For the most part, these early English sumptuary laws attempted to regulate consumption by regulating consumers themselves. There were some cases where attempts were made to secure enforcement by placing responsibility on the producers. One such case was that which penalized a tailor who cut cloth in violation of the regulations. This indicated the inability of constituted authority effectively to regulate the daily consuming practices of large numbers of people. As a result later sumptuary legislation has quite largely taken the form of laws which restrict or regulate the much smaller number of producers.

Sumptuary legislation in the New World is of much more recent origin and springs from quite different sources. In the absence of class distinctions in the United States there has never been any effort to regulate by law the type of clothing which one might wear, or the quality or amounts of food which might be consumed. In general this is still true, but in 1848 the people of Virginia were the first to find it necessary to protect themselves from predatory producers by passing a restrictive law. Imprisonment and fine were decreed for "any free person who shall knowingly sell any kind of diseased, corrupted, or unwholesome provisions, whether for meat or drink, without making the same fully known to the buyer" or "who shall fraudulently adulterate for the purpose of sale any drug or medicine, in such manner as to render the same injurious to health."[2] A similar law was passed by the state of Ohio in 1853.

With a growing population and increasing need for assurance of a pure food and drug supply it was quite logical that this type of regulation should develop first among the states. Later as the size of business firms increased and as their activities expanded beyond the boundaries of individual states, it was perfectly logical, likewise, that under our dual form of government the Federal government should join forces with the states to meet these changing economic conditions.

The Struggle for a Federal Pure Food and Drugs Law. It was not until about 1880 that the need for Federal regulation became apparent to a small number of forward-looking people. Until that time consumers lived a very simple life, many of them raising most of their own food, with practically all of them possessing the ability to judge its quality and purity by their own simple standards. As urban population expanded, these conditions changed. Cut off from sources of supply of fresh fruits and vegetables, consumers very naturally accepted the substitutes which enterprising businessmen began to supply in the form of canned and

[1] Baldwin, *op. cit.*, pp. 12, 29, 30.

[2] *Acts of* (Virginia) *Assembly*, 1847–48, "Criminal Code," chap. IX, p. 112.

preserved products. Inability of these urban consumers to judge the quality of processed fruits and vegetables, together with pressure to cut costs and thereby increase their profits, caused an increasing number of food packers to resort to adulteration and misbranding. At that juncture Dr. Harvey W. Wiley and his famous poison squad proved that such food preservatives as boric, salicylic, and sulphurous acids, benzoates, formaldehyde, sulphate of copper, and saltpeter are harmful and dangerous. At the same time, also, a thriving interstate business was being developed by the makers of many patent medicines. In some cases permanent customers were secured by the use of harmful, habit-forming drugs. Dr. Wiley estimated that newspapers and periodicals received $1,000,000 a year income for carrying the advertising of health-destroying and death-dealing products. By 1880 the situation had reached the point where an informed minority began to agitate for restrictive legislation to supplement ineffective state laws. This agitation continued for twenty-six years before public opinion could be aroused sufficiently to demand protection. For a quarter of a century a small group of entrenched interests was able to thwart all efforts to restrict their predatory activities. Ten years after agitation had begun, the first Pure Food and Drugs bill was introduced in Congress by Senator A. S. Paddock of Nebraska, in 1889. That bill passed the Senate but failed in the House. For many years similar tactics were followed. If a bill was introduced in one house of Congress the members voted for it in the double assurance that they would thereby gain consumer support and that the bill would never become law because it would die in committee in the other house. In twenty-six years 140 such bills were introduced and failed of passage.[1]

The Pure Food and Drugs Act of 1906

Provisions of the Act. On June 30, 1906, one of the last of the 140 Pure Food and Drugs bills rode through Congress and became law on the wave of President Theodore Roosevelt's trust-busting reform of big business.[2] The Act of 1906 declared it to be unlawful to manufacture

[1] Wiley, Harvey W., *An Autobiography*, especially chaps. 16, 17, Bobbs-Merrill Company, Indianapolis, 1930. For additional accounts of the legislative history of the first pure food and drugs law in the United States, see Toulmin, Harry Aubrey, Jr., *The Law of Food, Drugs, and Cosmetics*, W. H. Anderson Co., Cincinnati, 1942, and Wilson, Stephen, *Food and Drug Regulations*, American Council on Public Affairs, Washington, D. C., 1942, especially chap. 2.

[2] Cummings, Richard Osburn, in his *The American and His Food, a History of Food Habits in the United States*, University of Chicago Press, Chicago, 1940, gives credit to Upton Sinclair for arousing effective demand for purification of food supplies by writing his novel *The Jungle*. According to Cummings, Wiley's efforts prior to publication of Sinclair's book in 1906 aroused little public reaction and less legislative reaction.

in any territory or the District of Columbia, or to introduce into any state, any adulterated or misbranded food or drug. Administration was delegated to the Secretaries of the Treasury, Agriculture, and Commerce and Labor, while examinations of specimens were to be made by the Bureau of Chemistry in the Department of Agriculture. In practice the Department of Agriculture became the administrative agency. Sections 7 and 8 defined the terms "adulteration" and "misbranding." Section 10 provided for the seizure of adulterated or misbranded goods as a means of protecting consumers, in contrast with other penalty provisions which provided nominal fines and the possibility of imprisonment.

After its passage the act was amended several times. In the democratic reform period of 1912, under President Wilson, efforts were made to write a new law. Failing that, there was adopted the Sherley Amendment, which forbade fraudulent and false therapeutic claims on patent-medicine labels. That amendment was a direct result of a Supreme Court decision. The original Act of 1906 had declared a product misbranded if the label carried any statement that was "false or misleading in any particular." The Supreme Court had held that the phrase "in any particular" did not include curative claims. As introduced, the Sherley Amendment declared false and misleading claims to be illegal, but opponents succeeded in changing the word "misleading" to "fraudulent." This meant, of course, that it was almost impossible to enforce the provision. The following year Congress decreed that the net weight of every package must be stated plainly on the outside. In 1919 the Kenyon Amendment provided that wrapped meats were to be regarded as food in package form, and in 1923 a standard was set for butter. In 1930 the Secretary of Agriculture was authorized to set up minimum standards of quality, condition, and fill of canned goods except milk and meat products. The last amendment, in 1934, authorized the supervisory inspection of the sea-food packing industry for all those packers who asked for the service and were willing to pay for the inspection.[1]

From 1906 until 1940 the Department of Agriculture was the administrative agency. In the early days the Bureau of Chemistry supervised the inspectors. In 1927 research and enforcement activities were divorced, the Bureau of Chemistry and Soils being charged with research and analysis, while the Food and Drug Administration assumed responsibility for the enforcement of the Pure Food and Drugs Act, together with five other similar acts. In 1940, under Reorganization Plan IV, the Food and Drug Administration was transferred to the Federal Security Agency. This shift was in conformity with the plan of consolidat-

[1] *Laws Relating to Agriculture*, "The Food and Drug Act," June 30, 1906, as amended in 1912, 1913, 1919, 1927, 1930, pp. 144–152.

ing all Federal agencies concerned with public welfare, and particularly public health.

From the very beginning, lack of personnel hampered effective enforcement, a situation which continues under the revised organization. In an effort to spread the few inspectors as effectively as possible, a project method was adopted, designed to classify violations into those involving public health, those involving filth, and those which may be called economic violations. When it has been decided which projects will be given attention, practically all factories producing the particular foods and drugs are inspected, if access is permitted, since the law does not require a manufacturer to submit to inspection. If inspection reveals satisfactory conditions and methods, comparatively few samples are collected for analysis, but if unsatisfactory conditions or methods are found, more samples are taken, and if access to the factory is denied, its products are suspect, samples for analysis being taken as they enter interstate commerce.

Two types of action were used by the Administration, one against the goods themselves, the other against the manufacturer or distributor. The first type of action involved seizure of products in violation of the law as a means of protecting the consuming public. That type of action permitted speed in detecting and stopping violations. For example, if a carload of cabbages was received in a city and it was discovered that the shipment carried an excess of spray residue sufficient to endanger health, it might have been seized and destroyed within a comparatively few hours, whereas a criminal action would have required weeks, months, or even years to conclude. Seizure for misbranding frequently resulted in release of the goods for proper labeling. Since the only violation of the law was failure to comply with the negative labeling requirements, the goods were released under bond for such relabeling. Such action did not, however, prevent filing a criminal charge against the firm responsible for the violation. In 1939, the last full year of operation under the 1906 Act, there were 705 criminal prosecutions and 2,048 seizures. Administration inspectors at ports of entry rejected 2,795 shipments, while they inspected and released 13,557. In the course of their year's work, 30,832 parcels of food and 8,914 samples of drugs were collected and examined in the Administration laboratories.[1]

An Evaluation of the Act. Although the act was far from perfect there can be no doubt that millions of consumers of vast quantities of foods and drugs were much safer than they would have been without that protection. The act was designed to protect the *health* and the *pocketbooks*

[1] United States Department of Agriculture, *Report of the Chief of the Food and Drug Administration,* 1939, p. 6.

of consumers. In achieving the former aim it was much more successful than in achieving the latter. It was contended that harmful and grossly adulterated foods were comparatively rare under the act; certainly the situation was not as bad as that discovered and publicized by Dr. Wiley. It is difficult to imagine what conditions might have prevailed in the absence of legislation. Standards of quality in canned goods were higher, while interstate commerce in certain objectionable food products was suppressed. While some patent-medicine companies were forced out of business, others adopted the informal suggestions made by the Administration for improvement of their methods and products, with benefit to themselves and to consumers. Perhaps most important of all was the fact that for the first time in American economic life the Act of 1906 substituted the principle of *caveat venditor* for the previously prevalent rule of *caveat emptor*.[1]

It was in the field of economic values that the consumer continued to be exploited. Officials operating under the act were unable to prevent unscrupulous producers from palming off cheap and inferior goods on their customers. It is this phase of the law which requires further detailed analysis.

The Need for New Legislation

Weaknesses in the 1906 Act. Opposition of a small but powerful group which stood to lose if an effective act were passed and rigidly enforced resulted in making the Act of 1906 a compromise measure. When opponents found they were unable longer to prevent some form of legislation they sought to weaken it with qualifying terms. Further mitigation of its effects was sought and, according to Dr. Wiley, achieved by hampering and restricting enforcement activities. Quite obviously a good law is ineffective if unenforced. Dr. Wiley stated in his *Autobiography* that opponents of the law brought such pressure to bear on the Secretary of Agriculture and on President Theodore Roosevelt that a packed Board of Food and Drug Inspection was created to supersede the really effective work of the Bureau of Chemistry. In his words, "The Pure Food and Drugs Act was virtually repealed by executive edict."[2]

Starting out with such a handicap, the Act of 1906 always was administered by a small staff with an inadequate budget. Although the Food and Drug Administration was organized in 1927 to secure better enforcement, its appropriations were insufficient. The total fund at its disposal available for enforcement of six different acts was $2,457,980 in

[1] *Columbia Law Review*, vol. XXXII, "Consumers' Protection under the Federal Pure Food and Drugs Act," April, 1932, p. 723.

[2] Wiley, *op. cit.*, p. 241.

the fiscal year 1943. That was nearly $3,000,000 less than the amount requested at one time by officials for "reasonably satisfactory enforcement." It was smaller than the sums spent annually by some national advertisers whose products were subject to the provisions of the act. In 1943 there were seventy firms each of which spent one million dollars or more in advertising. Their total expenditures amounted to $212,000,000. One large food corporation spent $11,730,000 in advertising its products, all of which were subject to control by the Food and Drug Administration with a total appropriation of approximately one-fifth as much. One drug company spent nearly three times as much in advertising as the Food and Drug Administration was allotted for enforcement activities. The largest expenditure, amounting to $15,500,000, was made by a soap manufacturing company, while several manufacturers of dentifrices spent more than $1,000,000 each in their advertising.[1]

The annual volume of business in the food industry amounts to at least twenty billion dollars, while that of the drug industry is at least a half-billion dollars. For fourteen years of attempted prohibition enforcement $250,000,000 was spent by the Treasury Department; during that same period approximately $21,000,000 was spent by the Department of Agriculture to insure consumers a supply of pure food and drugs. The Federal Meat Inspection Act, also administered by the Department of Agriculture, is enforced by a staff of 2,400 inspectors, one being located in every packing plant, compared with the entire Food and Drug Administration staff of 806 charged with enforcement of six different acts. For enforcement purposes the Administration divided the nation into sixteen districts, for which only 154 inspectors were available. As a result only the grosser violations could be detected and prosecuted. Reduced to simple terms, the annual appropriation for the enforcement of the act amounted to approximately 1.5 cents per capita. Although the Administration modestly contended that "reasonably satisfactory enforcement" could be secured with a $5,000,000 appropriation, the very minimum which it should have had for effective enforcement was $18,000,000 or $20,000,000 a year. Even that sum would be small compared with the $2,130,000,000 spent for advertising in 1943, which amounted to a per capita cost of $15.66.

Experience has revealed continuous interference, by opponents of the act, with those charged to enforce it. Each one of the inspectors had to be constantly on the alert, for when the law was enforced powerful interests brought pressure to bear to force resignations or to secure

[1] *Printers' Ink*, February 4, 1944, p. 100.

changes in regulations or methods. For doing their duty they seldom received praise, but they frequently bore the brunt of undeserved condemnation.

To the difficulty of interference was added that of delay in court actions. Not only were inspectors hampered by their inability to enter factories where foods or drugs were being prepared, but when a case was established it might drag through the courts for years. Such a case was that of the B & M remedy, which was in litigation for ten years before a conviction was secured. Moreover, it was difficult to secure convictions in cases involving intangible deceptions or where political pressure was used.

Penalty provisions of the act were weak. The manufacture of an adulterated or misbranded product constituted a misdemeanor, the penalty for which was a fine not to exceed $500 or one year's imprisonment, or both, for the first offense, and a fine of not less than $1,000 or one year's imprisonment for each subsequent offense. Introduction into interstate commerce of an adulterated or misbranded product constituted a misdemeanor for which the penalty was a fine not exceeding $200 for the first offense and $300 for each subsequent offense, or imprisonment for one year. The imprisonment penalty was hardly ever used since it was practically impossible to prove personal responsibility of corporate officials for violations on the part of their firms. Fines were levied ranging from 1 cent to $4,500. A manufacturer of fraudulent patent medicines which were recommended for the treatment of such diseases as rheumatism, gout, inflammation of the kidneys, Bright's disease, and diabetes was fined 5 cents. At the other extreme was a fine of $4,500 levied against a manufacturer of substandard citrate of magnesia. The size of this fine indicates, of course, that he was a chronic offender. The Chief of the Food and Drug Administration expressed doubt whether "even these larger penalties were commensurate with the damage suffered by the consuming public through the purchase of such illegal products." The figures indicate that for certain types of offenders such nominal fines were regarded merely as a license fee for the privilege of continuing their business.

Critics of Administration enforcement officials have charged them with being more concerned not to disturb business than with protection of consumers. The officials defended themselves by pointing to the obvious limitations of the act and to their small operating budget. They contended also that co-operative methods were more effective than purely punitive enforcement. As late as 1930 Dr. Wiley contended that some practices permitted under the law were in direct opposition to its fundamental principle. There was too much tendency, he wrote,

to put enforcement in the hands of industries interested in foods and drugs.[1]

Incomplete Coverage of the Act. Upon examining the omissions of the act the need for new legislation was obvious. Advertising as we know it today was practically nonexistent in 1906, and consequently its regulation was not included. This meant that although manufacturers had to adhere to the truth in their labeling statements they were under no restrictions as to what they might say in their advertising. Like advertising, the cosmetic industry has had its greatest development since the Act of 1906 was passed. Courts having ruled that a cosmetic is not a drug, none of the many preparations offered for sale was subject to regulation. There are many curative devices contrived and offered for sale. As written, the act did not include them. Labeling requirements were entirely negative. The act required that the label had to contain truthful information but it need not and rarely did contain the whole truth. There was no requirement for food standards nor was there any control over factory production except that provided by the "shrimp Amendment" of 1934.

Efforts to Revise the Pure Food and Drugs Act of 1906

A Static Law in a Changing Nation. Almost from the date of its enactment the Act of 1906 became outmoded. It has been shown that although the need for pure-food legislation existed as early as 1880, none was passed for a quarter of a century. With the exception of several amendments the Act of 1906 continued to be the sole protection consumers had in a world a quarter of a century still further advanced. Modern consumers could scarcely be satisfied if they were restricted to the types of foods available in 1906 or if their clothing were cut to the fashions of that period. Neither would they wish or accept a 1906 model automobile, yet they continued to depend on a 1906 law for protection of their health and pocketbooks.

In 1912 efforts to revise the Act of 1906 were lost in a maze of other reform legislation, the net result being a weak amendment. During World War I and the following long postwar period no real effort was made to revise or rewrite the law. It was not until consumers were aroused as a result of their depression experiences that the Democratic party undertook in 1933 to include consumers in the New Deal program.

The method by which a bill becomes a law is a vastly different process than that imagined by many lay citizens. It is for that reason that the

[1] Wiley, *op. cit.*, p. 273.

following legislative history is presented. In theory, a Congressman who sees a need for legislative action introduces a bill which is referred to the appropriate committee for careful study. Receiving the approval of the committee, the bill is then returned to the Congress, where it is debated on its merits and ultimately passed. In practice, there are many devious steps between the introduction of a bill and the passage of a law. The following story is a striking illustration of the use of the legislative process to deprive consumers of the kind of a law which would have provided adequate protection in the purchase of foods, drugs, cosmetics, and devices.

A New Deal for Consumers—S1944. On June 6, 1933, the late Senator Royal S. Copeland, Democrat, of New York, introduced a bill "to prevent the manufacture, shipment, and sale of adulterated, misbranded food, drugs, and cosmetics, and to regulate traffic therein; to prevent the false advertisement of food, drugs, and cosmetics, and for other purposes." This became known as Senate Bill 1944, and was referred to the Committee on Commerce and by it to a subcommittee of three. At that time Dr. Rexford Tugwell was serving as Undersecretary of Agriculture. As a part of the general New Deal program he secured the support of Secretary Wallace for a new Federal Pure Food and Drugs Act and together they enlisted the aid of President F. D. Roosevelt. The bill was drafted in the Department of Agriculture, largely in the Food and Drug Administration. The experience of twenty-seven years was reflected in the first draft, it being so drawn as to substitute strength where there had been weakness and to include specific provisions where there had been omissions. Senator Copeland, a medical doctor, was the only member of the Senate who would accept responsibility for introducing the bill. He served as chairman of the subcommittee which held hearings, but at the same time he was giving health talks on a radio program sponsored by Fleischmann's Yeast Company, an affiliate of Standard Brands, Inc., whose advertising would not have stood the tests imposed by the bill. In fact this was one of the first companies against which the Federal Trade Commission proceeded in 1938 under the amendment authorizing it to regulate advertising. Yet those close to the legislative battle seem to agree that Senator Copeland worked assiduously for his bill.[1]

S1944 included regulation of cosmetics and curative devices; forbade false advertising of foods, drugs, and cosmetics; required definitely informative labeling, and promulgation of standards; provided for operation of factories under Federal permit, if necessary; prescribed more

[1] Cavers, David S., "The Food, Drug, and Cosmetic Act of 1938: Its Legislative History and Its Substantive Provisions," in Duke University Law School's Journal *Law and Contemporary Problems*, vol. 6, Winter 1939, p. 10.

severe penalties; and in other ways enhanced the powers of the Food and Drug Administration.

Public hearings were conducted on December 7 and 8, 1933. Of the 84 witnesses who were heard or who submitted briefs, 17 appeared for consumers and one group submitted a memorandum. Of the 17 who appeared, 4 were government officials, including the Secretary of Agriculture and the Chief of the Food and Drug Administration. Of the 504 pages of testimony, 114 were devoted to a presentation of the case for the bill. Of that number 66 pages were accounted for by government officials, and most of them (57) carried the testimony of the Chief of the Food and Drug Administration. Representatives of Consumers' Research appeared to support the bill, but without enthusiasm.[1]

Opposition, Compromise, and Delay. Among the major changes proposed by the bill, inclusion of cosmetics was quite generally accepted. Likewise, the need for some control of advertising was granted, and there was no serious opposition to the proposed increased penalties.

There was, however, vigorous opposition as revealed through 390 pages of testimony by 67 witnesses. One of the sections around which opposition centered was that dealing with administrative provisions, it being charged repeatedly that the bill proposed to give to the Secretary of Agriculture autocratic, czaristic powers. It was argued that Congressional delegation of such powers was unconstitutional. The provision for factory inspection and control was bitterly assailed as un-American and unconstitutional. The nature of the opposition to food standards has been indicated in Chapter 25. Considerable alarm was expressed over the proposal to make corporate officials personally liable in criminal actions involving violations.

The proprietary interests argued that the bill, if it were to become law, would interfere with the free right of self-medication, although the purpose of the bill was to render self-medication safer. Advertising interests contended that their vast industry would be doomed. Of all the objections this was perhaps the weakest, for the bill simply outlawed false and misleading advertising. To argue therefore that advertising would be doomed was to argue that all advertising is false and misleading. The argument was well summarized by Secretary Wallace when he stated bluntly that "advertisers can tell the truth and still do business profitably." Patent-medicine producers viewed with genuine alarm the proviso that their labels should tell the whole truth. To reveal their formulas would be to reveal the secrets on which their business depended. Witnesses for consumers gave the obvious reply that the bill was drawn to

[1] United States Senate Committee on Commerce, Seventy-third Congress, Second Session, *Hearings on S1944*, Government Printing Office, Washington, 1934.

protect consumers rather than producers and that consumers had a right to know what was contained in proprietary packages. Closely related to this argument was the contention of proprietary-medicine men and manufacturers of curative devices that the provisions of the bill affecting them were part of a vicious scheme of the "medical trust," represented by the American Medical Association, to drive them out of competition.

It was argued by those who regarded some change as inevitable that the Act of 1906 should be amended rather than a completely new act written. In that way the benefits of twenty-seven years of court decisions could be retained. Mr. Campbell, Chief of the Food and Drug Administration, pointed out that although the bill had been completely rewritten, the terminology of the 1906 Act had been used wherever feasible. A similar objection was that forty-two states had passed pure food and drugs laws patterned after the Federal statute. Just why changing the pattern would be disadvantageous was not made clear. The advantage would seem rather to run in the opposite direction, for if the Federal government were to assume the lead in modernizing its legislation the states would be encouraged to make the necessary changes in their laws.

Another argument used by those who regarded a change as inevitable was that the advertising control should be given to the Federal Trade Commission rather than to the Food and Drug Administration. According to *Business Week* this tactic was based on the theory that if it succeeded the Administration and the Commission would be at odds and there would be very little if any real advertising regulation. There was a plausible basis for the proposal, of course, in the fact that such control of advertising as we then had was exercised by the Commission. As a matter of fact, records of the Commission show that their advertising cases involving food and drug products were extremely rare. Viewed objectively, it would seem that the logical body to control advertising is the one that has authority for controlling the content of food and drug products and their movement in commerce.

Compromises followed the hearings. An advertising trade paper wrote editorially that "as a result of many a long and secret conference which representatives of the industries concerned held with the Senator, with officials of the Food and Drug Administration, even with the President himself, many objectionable provisions were deleted. . . ." The original bill was amended in several important respects and reintroduced as Senate Bill 2000. Among the important compromising provisions was one which proposed to limit the administrative powers of the Chief of the Food and Drug Administration and of the Secretary of Agriculture by the use of committees on which representation was to be accorded to

the manufacturers of products which were to be under control. The provision which had required makers of patent medicines to print their formulas on the labels was deleted entirely. There had been a provision prohibiting therapeutic claims contrary to the consensus of medical opinion. This was changed so that such claims, instead of being prohibited, were declared to be a form of misbranding if they were not supported by substantial medical opinion or by demonstrable scientific facts. The requirement that a palliative be labeled as not a cure was changed to compel the labeling to show how the palliation is effected. The section on voluntary inspection service was deleted, as well as that authorizing investigations through the medium of the Federal Trade Commission Act. An innovation in the new bill was the provision authorizing the enforcing agency to accept plans of representative advertising associations for the self-regulation of advertising practices.

These concessions were insufficient to allay the fears of the food, drugs, and cosmetics manufacturers. So unsatisfactory was the bill that no hearings were ever held. By direct representations to Senator Copeland their objections were made sufficiently strong so that he revised the bill again, introducing it on the floor of the Senate on February 6, 1934, as Senate Bill 2800. The new bill was submitted to the Committee on Commerce, which ordered hearings to begin on February 27. These continued until March 3 and were conducted by the full Committee. In the course of the several Committee sessions 110 witnesses appeared and 666 pages of testimony were taken. Of the 110 witnesses less than 10 represented ultimate consumer interests and three of those were as vigorous in their opposition to the bill as the most thoroughly frightened patent medicine or cosmetic concoctor. Through their associations opponents of the bill raised a fund of $500,000 to secure its defeat. Newspapers in the country were lined up in opposition to the bill by threats from advertisers that advertising appropriations would be discontinued or severely reduced if the bill were to become law. According to *Business Week*, Senator Copeland was very amenable to the suggestions made by Charles Wesley Dunn, counsel for the Associated Grocery Manufacturers of America and the American Pharmaceutical Manufacturers' Association:[1]

> "Naturally, Mr. Dunn does not expect the Senator to restore any of the troublesome provisions disposed of last year (quality standards, voluntary inspection service, the 'inference and ambiguity' definition of false advertising, bans on the advertising

[1] *Business Week*, December 15, 1934, p. 21. A detailed legislative record has been written by Mr. Dunn under the title *Federal Food, Drug, and Cosmetic Act*, G. E. Steckert & Co., New York, 1938.

of any curative claims in the treatment of specified diseases, etc.). Among the important additions and deletions which he would like to see are:

(1) Elimination of all formula disclosure provisions.
(2) A guarantee of protection for 'harmless trade puffing.'
(3) Exemption of proprietary foods from all standards requirements.
(4) Limitation of penalty for refusal to permit government inspection.
(5) Liberalization of drug adulteration and misbranding definitions.
(6) Modification of publishers' and dealers' exemption to provide penalty for willful participation."

The combination of opposition, compromise, and delay succeeded in killing S2800. While the Food and Drug Administration and most of the women's organizations were willing to accept the bill in spite of its weaknesses, witnesses for Consumers' Research and the People's Lobby would have none of it. A model bill prepared by Consumers' Research was introduced on the floor of the House by Representative Boland as HR8316, while representatives of industry had the sort of bill they wished to support introduced as HR6376. S2800 was killed not only by its enemies, but by friends who wanted a better law than that then on the statute books. On one occasion there was slight discussion of the bill on the floor of the Senate, but it died without coming to a vote.[1]

S5—A Bill Nobody Wanted. A curious struggle for a modern law regulating food, drugs, and cosmetics continued in the Seventy-fourth Congress. January 3, 1935, Senator Copeland introduced Senate Bill 5. This was a modification of S2800 amended in the interests of those it was supposed to regulate. So thoroughly was it amended in fact that practically all consumer interests opposed it. Although the Chief of the Food and Drug Administration did not appear as a witness against the bill, neither did he support it. The best that could be said for it was that perhaps it would be a better law than the one in effect, since it included cosmetics and some control of advertising. On the other hand, critics of the bill contended that consumers would have actually less protection if the bill were to become law than they then had under the act of 1906.

In spite of the almost complete consumer objection to the bill, witnesses for those who were supposed to be regulated were not satisfied. They wanted still more teeth removed from the proposed law and sought to accomplish their purpose by submitting two bills of their own. One

[1] United States Senate Committee on Commerce, Seventy-third Congress, Second Session, *Hearings on S2800*, Government Printing Office, Washington, 1934.

of these was drawn by Mr. Dunn, whose connections have been given, and the other by the representative of the Proprietary Association. Proponents of these bills were frank in admitting that they were submitted without any idea of passage but as a means of still further whittling away the already emasculated proposals for regulation.

In the new Congress, Senator Copeland had become chairman of the Committee on Commerce. In that position it might have been expected that he would exercise powerful influence in favor of the bill which he sponsored. The record shows, however, that instead of conducting hearings by the whole Committee under his chairmanship, a subcommittee was appointed under the chairmanship of Senator Bennett Champ Clark, an avowed and vigorous opponent of any change in the law pertaining to food and drugs. Referring to this Committee appointment and to the hearings which were held March 2, 8, and 9, *Business Week* commented as follows:[1]

> "Because he presented his constituents' demands with considerable vigor, Senator Clark was named by Committee Chairman Copeland to preside at the hearings. Food and drug fight fans have since found several other reasons to explain this puzzling appointment of a man whose opposition to the bill has thus far been unrelenting. He is a high-pressure parliamentarian, can rush the hearings through in 2 days (other hearings dragged over a total of 11 days). Industry representatives think he will be able to choke off propaganda of the consumer-agitation type, which was the one thing they feared about hearings."

In contrast with the large number of witnesses appearing in previous hearings, there were only 69, whose testimony is recorded in a 372-page summary. Most of the witnesses represented industry. The Chief of the Food and Drug Administration appeared and spoke perhaps three minutes, giving perfunctory support to the bill. This oral testimony was followed by a more detailed brief. Among the amendments to which consumer witnesses objected most vigorously and unanimously were those which proposed to turn over administration to committees representing the regulated industries, and the modified seizure provisions which would have made the proposed law actually weaker than the one then in force. Objection was registered also to the ineffective control of advertising, the failure to require listing of cosmetic ingredients, and the complete deletion of provisions for standards.

Although Senator Clark did not succeed in rushing the hearings

[1] *Business Week*, February 23, 1935.

through in two days he did terminate them at the end of the third day.[1] On March 26, the bill was reported favorably to the Senate and placed on the calendar. In a surprise move early in April, Senators Bailey and Clark pushed through four amendments which so thoroughly weakened the bill that its passage in amended form would have given predatory producers more freedom and consumers less protection than they enjoyed under the 1906 law. Even Senator Copeland was so dismayed that he recalled the bill and had it placed back on the calendar. It came to a vote again on May 28, and was passed with amendments submitted by Senators Bailey, Clark, and Vandenberg. One of these amendments weakened the advertising clause, another emasculated the provision for injunctions, while the third, prohibiting multiple seizures of goods in violation of the Act, was hailed by the patent-medicine manufacturers as their "bill of rights."

The House referred the bill to the Committee on Interstate and Foreign Commerce, which held protracted hearings during the summer, offering still further opportunities to opponents of the proposed legislation. When the bill was returned to the House it had been strengthened generally. The House Committee had reinstated the provision requiring compulsory grade labeling and had rejected those Senate amendments which sought to turn administrative control over to committees and to weaken enforcement by restricting powers of seizure.[2] The bill was weakened by the House amendment to transfer control over advertising to the Federal Trade Commission. This amendment represented a tactical victory for opponents of the bill, particularly the Proprietary Association. It is this latter group which most fears any effective advertising control and which sponsored the Federal Trade Commission proposal in the belief that divided counsels would result in ineffective regulation.

In its amended form the bill was reported favorably to the House early in 1936. There was still opportunity for it to become law, if passed by both House and Senate. On June 19, 1936, the bill was passed in amended form by the House. It was referred to a conference committee which was thoroughly snagged by the several amendments, particularly the one concerning advertising control. Congress adjourned on June 20, leaving the country's consumers to the mercies of a thirty-year-old law. Advertising agencies, publishers, and cosmetics manufacturers who were still free from any national regulation were delighted with the outcome.

[1] United States Senate Committee on Commerce, Seventy-fourth Congress, First Session, *Hearings on S5*, Government Printing Office, Washington, 1935.

[2] United States House of Representatives, Committee on Interstate and Foreign Commerce, Seventy-fourth Congress, First Session, *Hearings on HR6906, HR8805, HR8941, and S5*, Government Printing Office, Washington, 1935.

Some of those who were still regulated by the 1906 law were actually disappointed that S5, as amended, failed of passage, for in certain respects its provisions would have been much more lenient than those under which they then operated.

Consumers Get a New Pure Food Law

The Federal Food, Drug, and Cosmetic Act of 1938. Undaunted, Senator Copeland introduced a new Senate Bill 5 in the Seventy-fifth Congress, January 5, 1937. As amended by Senators Bailey, Clark, and Vandenberg, the proposed legislation was less effective than the Act of 1906. Nevertheless, the Senate voted to pass the amended bill on March 8, 1937. Although the House merely marked time while the Senate was deadlocked for six months over the proposed legislation for reorganization of the Federal courts, no action was taken on the Food, Drug, and Cosmetic Bill.

It appeared that opponents of legislation drawn to protect consumers had won a final victory. With staunch friends in the Senate and a difference of opinion between the Senate and the House concerning advertising control, there seemed to be little, if any, probability that a change would be made. After four years of effort consumers were left in a streamlined age with a 31-year-old law.

At that juncture at least two significant developments occurred. There were many businessmen who doubted the wisdom of the opposition to a law so obviously needed. They particularly questioned the wisdom of the tactics which had been used with temporary success. It was feared that a reaction would result in a wave of state laws whose severity would make advertisers and cosmetics manufacturers regret their opposition to a lenient Federal law. Already eight new bills, patterned after the various Copeland measures, had been introduced in state legislatures and it was expected that similar measures would be introduced in other states. The situation was viewed with alarm in the *Drug Trade News*. The state of Maine passed a law in 1935, for the regulation of cosmetics, which forbids the sale within that state of any cosmetic preparation which has not been registered and granted a certificate by the Department of Health and Welfare.

Louisiana was the first state to place the manufacture of food, drugs, and cosmetics under modern rigid regulation. Control of advertising is included in the law.

These laws and the possibility of others like them being enacted gave serious concern to thoughtful manufacturers. With their modern large-scale production methods maintained by a system of national marketing, uniformity is essential. The question with which they were faced was

whether their standard of uniformity would be that which meets the new, rigid requirements of Louisiana or would instead be geared to unregulated markets. If the latter, then their products could not be sold in Louisiana. If such states as California, Connecticut, Montana, New York, North Dakota, Texas, Washington, and West Virginia were to pass the bills which had been introduced in their legislatures the national market would be severely restricted for those who did not meet the new requirements. Also there would be the problem of conflicting provisions among the various state laws. Publishers for national circulation would be compelled to meet the advertising control laws of such states on penalty of being denied the privilege of selling their newspapers and magazines within the state borders. The predicament in which manufacturers found themselves and for which they were largely responsible was well summarized in a trade journal:

> "It is time that all the manufacturers of foods, drugs, and cosmetics, as well as the publishing and broadcasting interests deriving large revenues from one or more of these industries, faced the music. A new and more drastic Food, Drugs, and Cosmetic Act is going to be enacted whether some few factors in the industry like it or not, and the sooner the law is enacted the better it will be. Those who fostered the fight between the Senate and the House over the question of advertising jurisdiction probably thought they had performed a great feat. If they continue to perform such stunts in an effort to block the bill, the entire industry will find itself in such a maze of state legislation that these people will wish they had played the game square."[1]

A second development occurred during September and October of 1937 when, in 15 states, at least 73 persons died as a direct result of taking the drug known as "Elixir Sulfanilamide," while twenty others who took the "elixir" also died, although in their cases it was not possible to place sole responsibility on the drug. Before marketing the "elixir" the manufacturer tested it for flavor but not for its effect on human life. Deadly though the preparation proved to be, there was no provision in the Act of 1906 on which enforcement officials could proceed except that of misbranding. If the product had been labeled a "solution" instead of an "elixir" the Administration would have been powerless. The full import of that situation was realized when an official report revealed that of the 240 gallons manufactured no more than 6 were sold and consumed and were responsible for the 93 deaths. In other words, in the absence of seizure by the Food and Drug Administration there might have been 3,720 deaths. Criminal action resulted in combined

[1] *Drug and Cosmetic Industry*, August, 1936.

fines amounting to $26,100, the heaviest financial penalty ever imposed under the Act of 1906. In response to a Senate resolution the Secretary of Agriculture submitted an official report, including recommendations for adequate legislation.[1] Not long thereafter, Senate Bill 5 was revived and reported favorably by the House Committee on Interstate and Foreign Commerce. Following passage by the House in altered form, a Conference Committee finally reached agreement, the House having meantime won the struggle over advertising control, and Senate Bill 5, revised and amended, became the Federal Food, Drug, and Cosmetic Act, on June 25, 1938, effective twelve months later.

But the battle was not over. The next step in the campaign of strategic defeat was that of securing postponement of the effective date. It appears that some of the manufacturers who would have been most affected by the new law put pressure on certain Congressmen to delay the date when it would go into effect. In this they were successful, although the Food and Drug Administration and reputable manufacturers insisted that no postponement was necessary. The new act did not go fully into effect until July 1, 1940.[2]

On the other hand, the Food and Drug Administration began a campaign against dangerous cosmetics within three weeks after approval of the new act. That campaign resulted in 85 seizures and 49 criminal prosecutions in 1939. As a result, by 1940 the market was cleared of such dangerous products, with one exception, and continuous surveillance together with changed formulas kept the market clear for consumers.

Consumer Gains under the New Law. After five years of legislative struggle what kind of law was passed? In seeking to answer this question it will be helpful first to indicate those provisions which extend and strengthen the powers of the Food and Drug Administration, as the enforcement agency directly concerned with consumer welfare.

In the first place the new act is more inclusive. In addition to food and drugs, cosmetics and curative devices are brought under control. Sections 601 and 602 define adulterated and misbranded cosmetics, requiring, among other things, that labels bear positive information and that the container must not be so made, formed, or filled as to be misleading.

Secondly, the act extends the existing control over food. For example, foods that are dangerous because of naturally contained poisons, as well as those containing added poisons, are subjected to regulation. Defini-

[1] United States Senate, Seventy-fifth Congress, Second Session, Document No. 124, *Elixir Sulfanilamide*, Government Printing Office, Washington, 1937.

[2] Harding, T. Swann, "Congressional Medicinal Show," in *Christian Century*, vol. LXI, p. 851.

tions and standards of identity are provided, making possible effective control, as has been true for butter. The purpose of that section is to promote honesty and fair dealing in the interests of consumers. By 1943, 89 different food standards had been promulgated. The Act provides that producers may appeal to the courts, and eleven had done so, but no regulation had been held invalid. An important case involving the definition and standard of Farina and Enriched Farina was carried to the United States Supreme Court, where the Administration was upheld.

A food product is declared to be adulterated if it has been prepared, packed, or stored under insanitary conditions, and where the act may be ineffective in protecting the public health against bacterial contamination of food, temporary license restrictions can be imposed until the condition is corrected. Acting under this power, the Administration seized more than 10,000 tons of food products in 1942 because of serious contamination with filth. Most of that adulteration was avoidable, resulting from inexcusably careless handling and storage. Labels must contain positive information as to composition and quality of foods, particularly in the case of special dietary food, such as that for infants and invalids. The new act eliminates the distinctive name clause of the old law, under which many cheapened and debased foods had escaped control. A food product is adulterated if it contains any coal-tar color not certified by the Secretary as harmless and suitable for use in food.

Likewise, the new act extends control over drugs. The "Elixir Sulfanilamide" tragedy led to the inclusion of Section 505, which requires that new drugs be adequately tested for safety before being offered for sale. Drugs intended for diagnosing illness or for remedying underweight or overweight or for otherwise affecting bodily structure or function are subjected to regulation. Under a 1941 amendment all insulin distributed within the jurisdiction of the Federal law must be certified by the Food and Drug Administration. A drug is declared misbranded if its label fails to give adequate directions for use and adequate warnings where its use may be dangerous to health if taken in the dosage and with the frequency prescribed by the manufacturer. Drugs containing specified ingredients must be labeled "Warning—May be habit-forming." Likewise, powerful drugs which may be misused must carry label warnings against probable misuse. Special safeguards are provided for packaging and labeling drugs subject to deterioration. Preparations such as mouth washes must conform to label statements as to strength, purity, and quality. It is no longer necessary that the Food and Drug Administration prove that a manufacturer knows his labels are false, as under the old law. This strengthens enforcement procedure, particularly in the field of patent medicines. Several provisions

apply alike to cosmetics, food, and drugs, such as the section requiring packaging under sanitary conditions, and the one pertaining to the use of certified coal-tar colors.

Administrative and enforcement provisions are strengthened along four fronts. Officials are authorized to inspect factories which make interstate shipments, and common carriers are required to give enforcement officers access to shipping records for the purpose of establishing Federal jurisdiction. Federal district courts are given jurisdiction and authority to restrain violations by injunction. Penalties are made much more severe. A first offense draws a possible fine of $1,000 and/or imprisonment for one year, while subsequent violations may be penalized by a fine of $10,000 and/or three years' imprisonment.[1]

Limitations of the New Law. The first six chapters of the Federal Food, Drug, and Cosmetic Act provide improved protection for consumers, but it was feared that Chapter 7 dealing with general administrative provisions might partially nullify the preceding chapters.

After giving the Secretary of Agriculture authority to promulgate regulations for the efficient enforcement of the Act, it was provided that the Secretary, either on his own initiative or upon application of any interested industry, or substantial portion thereof, *shall*[2] hold a public hearing upon a proposal to issue, amend, or repeal any regulations. After a hearing, the Secretary is required to publicize his action in issuing, amending, or repealing the regulation, but it is provided that no such order shall take effect prior to the ninetieth day after it is issued. It was feared that this provision might enable obstructionist groups to delay enforcement.

Nor was that all. It was provided further that affected members of an industry might file a petition with the Circuit Court of Appeals in the district wherein they reside or had their principal place of business, calling for judicial review. The next paragraph of the Act entitles the petitioner to bring in additional evidence not presented at the hearing before the Secretary. The Court may then affirm the Secretary's order or set it aside, temporarily or permanently, and the decision of one circuit court is binding for the entire country.

At the time these provisions were written into the law there were many proponents of strong food, drug, and cosmetic legislation who feared that the Act would be seriously weakened and consequently they opposed passage of the law with those provisions. In practice, the

[1] United States House of Representatives, Seventy-fifth Congress, Third Session, Report No. 2139, *Food, Drug and Cosmetic Act.* Also *Federal Food, Drug and Cosmetic Act,* Public, No. 717, 75th Congress, Chapter 675, 3d Session.

[2] Italics supplied.

procedural and review provisions have slowed the process of prescribing regulations and they have caused delays in the effective operation of some regulations, even beyond the 90-day period specified in the law. Of the 11 cases taken to court by 1943, only one was held invalid by a Circuit Court of Appeals and in that case the decision was reversed by the United States Supreme Court. In an effort fully to meet the intent of the law with reference to hearings, the Administration has spent considerable time in drafting the definitions and standards for foods. Hearings lasting several weeks are not uncommon. This time-consuming process is not only expensive, but frequently seems scarcely justified by the importance of the issues involved. On the other hand, the knowledge that court action may follow has served to encourage very careful and detailed analysis of the facts on which each regulation depends. It has been observed also that the process of cross-examination of witnesses and presentation of conflicting interests within the industry have had the effect of modifying the more extreme claims of particular parties or groups.

Other Federal Regulatory Agencies

Federal Trade Commission. Enacted originally for the purpose of preventing unfair methods of competition and unfair or deceptive acts in commerce, the Federal Trade Commission has become increasingly concerned with protection of consumers. Undoubtedly its most important recent assignment in the area of consumer protection involved the power granted in 1938 to protect consumers from false and misleading advertising. The activities of the Commission in this field have been described in Chapter 11. It is important to add at this point, however, that any consumer may file a complaint concerning advertising, either by letter or in person. Another important activity recently assumed by the Commission is that of enforcing the Wool Products Labeling Act, the nature of which was described in Chapter 25. Closely related to the enforcement of that Act is the work of the Commission in establishing trade practice conference rules concerning informative labeling. As a result of conferences of industry members, rules regulating trade practices are agreed upon and promulgated by the Commission. Under this arrangement, the rayon, silk, and hosiery industries, as well as fur garments and fur products industries, are operating under rules which require the disclosure of information identifying the fibers in the products.[1]

Department of Justice. Passed in 1890, the Sherman Anti-Trust Law has always been regarded as a device for breaking up monopoly, but

[1] Federal Trade Commission, *Protection of the Consumer;* also *Annual Reports.*

without establishing the connection between the law and ultimate consumer protection. In fact, the law has rarely been enforced consistently. There have been long periods when it was scarcely enforced at all. Beginning in the late 1930's under the leadership of Assistant Attorney General Thurman W. Arnold, an effort was made to establish a policy of consistent and rigorous enforcement. This was done not simply to break up isolated monopolistic practices, but rather to maintain a free competitive market so that consumers might have the advantage of competitive in place of monopolistic prices. An illustration of the immediate and direct effect of anti-trust enforcement is found in an indictment of milk producers, distributors, and drivers in Chicago. Immediately milk prices which had been from ten to twelve cents a quart fell to eight or nine cents. When the court sustained a demurrer, the price of milk rose; but when, on appeal, the Supreme Court upheld the indictment, the price in stores again fell to eight cents. It is estimated that the resulting annual savings to store customers is at least $3,000,000 to $4,000,000.[1] The annual reports of the Assistant Attorney General contain additional illustrations of the way in which the Department of Justice operates as a regulatory agency in part at least for the benefit of consumers.

Other Agencies. There are at least eight other Federal agencies whose activities are in part indirectly beneficial to consumers. For example, the Federal Communications Commission is charged with the important task of regulating interstate and foreign commerce in communications by wire and radio. The rates which consumers pay for communication services, as well as the type of service received, are in large measure dependent upon the activities of this Commission. Millions of consumers use the commercial and savings banks of the nation as individuals and in that capacity need protection. The large number of bank failures in the depressed 1930's led to the creation of the Federal Deposit Insurance Corporation whose chief function is to insure the deposits of all banks which are entitled to the benefits of insurance. If a bank is closed without adequate provision having been made to pay the claims of depositors, the Corporation acts as receiver and pays off the depositors up to a maximum of $5,000. A recently assumed regulatory activity is that of the Board of Governors of the Federal Reserve System in regulating the terms under which consumer credit may be extended by merchants and lenders. Although inaugurated as a wartime measure, it is not unlikely that this control may be extended indefinitely into the future. For many years the Interstate Commerce Commission has exercised increasing control over the transportation systems of the nation. Although the large

[1] Edwards, Corwin, "Consumers and Monopoly Problems," in *Making Consumer Education Effective*, p. 218 Stephens College, Columbia, Missouri, 1940.

users of transportation are commercial interests, individuals are affected directly when using railroads, busses, boats, and airplanes for passenger service and indirectly when the commodities they purchase are shipped by these various means. The Commission is charged with the duty of determining whether just, reasonable, and nondiscriminatory rates are maintained by carriers under its jurisdiction; it has authority to prescribe such rates, fares, and charges as it finds to be reasonable and just. Moreover, it exercises authority over the safety appliances in use on American railroads. The Office of Price Administration is charged with the wartime task of preventing an inflationary rise of prices. The benefits flowing from a successful execution of that assignment are general, but there are many aspects of its work which are directly beneficial to consumers. These will be examined in greater detail in Chapter 29.

An important division in the Post Office Department is that which undertakes to prevent the use of the mails to perpetrate fraud or to carry on lotteries or to use the mails for the transportation of indecent printed matter. The Securities Act of 1933 requires a full and fair disclosure to investors of the material facts regarding securities publicly offered and sold in interstate commerce or through the mails and to prevent fraud in the sales of securities. The Securities and Exchange Commission is charged with the enforcement of that act and its activities are indirectly beneficial to investors. Among the activities of the Alcohol Tax Unit in the Bureau of Internal Revenue, Treasury Department, is that of administering the regulations concerning the labeling and advertising of distilled spirits, wines, and malt beverages entering interstate commerce. In the same Department, the Bureau of Narcotics is charged with the prevention of violations of the Federal Narcotic and Marihuana Laws and of the Opium Poppy Control Act of 1942.

State and Local Consumer Protective Laws

Policing Business for Consumers. Every state constitution grants to the legislative body a broad police power under which laws may be enacted for the protection of public health, morals, and welfare. The broad scope and coverage of such legislation is far greater than is generally realized. There are, for example, laws governing sanitary conditions through which goods and services are produced, such as those requiring sanitary inspection of dairies and restaurants. There are laws which are designed to compel special treatment of products so as to render them more safe. Illustrations of such control include city ordinances requiring that all milk offered for sale be pasteurized, and state ordinances stipulating that all hair and feathers used in mattresses must be sterilized. There are laws against harmful ingredients in food or drugs. State and local laws

forbid adulteration of food and drugs. City ordinances commonly forbid the sale of food unfit for human consumption. Most cities have sanitary regulations covering stores, bakeries, and meat shops. Among businesses dispensing personal services are barber shops, beauty parlors, and bathhouses, all of which operate under more or less rigid sanitary regulations. In recent years housing regulations have become more rigid. Today most cities fix minimum standards of lighting, air, and sanitary facilities in all buildings leased for residential purposes.

It is obvious that state and local laws enforced by state and local agencies are needed to supplement Federal control. Not only do conditions vary from state to state and city to city, but in many cases Federal control would be unconstitutional. On the other hand, local control may very likely be rendered ineffective because of the strong influence of organized business groups. On the national scene these groups would exercise much less influence.

The Problem of Dual Control. Under the American form of government there are 49 sovereignties with several thousands of additional municipalities exercising limited authority. This situation precipitates the question as to which of the three governmental agencies shall attempt to regulate the production, advertising, and sale of food, drugs, and cosmetics. Constitutional restrictions, dividing authority, sometimes operate to hamper the passage and enforcement of laws designed to protect consumers. The Federal government is unable to regulate commercial activities confined to a single state, while a state in turn is powerless to regulate commercial activities which cross state lines. There is a fear among states, also, that too stringent regulation on the part of one state will antagonize business interests, discouraging the undertaking of new business and perhaps encouraging established firms to move to other states. This fear is probably more apparent than real, but nevertheless it plays its part in dampening the ardor of legislators for bills to protect consumers.

The possibility of securing consumer protection by state laws has been suggested, as has the possibility that a few scattered state laws may be as effective as a Federal law. The probability runs in the other direction, however. The trend in American manufacturing and merchandising is definitely toward integrated manufacturing with national advertising and national distribution through national chains. This means that all commerce tends to become interstate and therefore subject to Federal control. The annual reports of the Federal Food and Drug Administration reveal a growing degree of co-operation between the Federal and the various state regulatory agencies. One major difficulty in the way of greater co-operation is the lack of uniformity in state laws and in the

agencies which enforce them. As of 1939 it was reported that all states, with the exception of New Mexico, had laws regulating the manufacture and sale of adulterated and misbranded food and drugs. In 17 states these laws were enforced by boards of health; in 11 states by departments of agriculture; by independent commissions in 15 states; and by agricultural experimental stations in 4. Per capita appropriation for enforcement of state laws in 1937 varied from 0.24 cents in California to 17.28 cents in Wyoming. In the same year the Federal appropriation for the Food and Drug Administration amounted to 1.33 cents per capita.

The Association of Food and Drug Officials has proposed a model state food and drug act which has been adopted in Indiana, and, with slight variations, in Florida, Nevada, and North Carolina. The model bill requires the state standards to conform with Federal standards as far as practicable. Federal standards for foods are automatically incorporated in the statutes of 13 states.[1]

While most of the states have some kind of regulations for foods and drugs, only five have passed laws regulating the sale of cosmetics. Some of these are not very effective, one requiring only that the label bear the name and address of the manufacturer. In Maine, registration may be refused to any cosmetic which contains injurious substances. In 1942 9,958 certificates were issued, registration being denied to 5 preparations. Louisiana, Virginia, and North Dakota have laws which are almost identical with the Federal act of 1938. In accordance with its established practice of publicizing the findings of its surveys, the State Laboratories Department of North Dakota made a state-wide survey of cosmetics, deodorants, and anti-perspirants. Copies of the report are available to the citizens of the state and are valuable buying guides. Reading the report, a North Dakotan would learn the differences between deodorants and anti-perspirants; the materials out of which each are made; the active ingredients and their effects upon the skin; likewise their effects upon clothing; and the likelihood that they would have any irritating or deleterious effects. The reader would learn that all samples examined in the North Dakota survey were misbranded, according to the regulations of the North Dakota law. By brand name and manufacturer, the results of the tests are given in tabular form showing the net weight, the cost per ounce, the moisture, and the ash content. The table shows that the cost per ounce of nine nationally advertised deodorants ranged from 32 cents to $1. The label of one product claimed that it stops underarm perspiration, removes odor, does not rot clothes, can be used after shaving or as a depilatory, and may be used daily if

[1] Arizona, California, Idaho, Maryland, Michigan, Mississippi, Missouri, Nevada, New Hampshire, Oklahoma, Utah, Vermont, Wyoming.

necessary. The State Laboratories Department reports that the active ingredients of that product were not stated, that it is not a deodorant, that it should not be used after shaving or as a depilatory, that daily use may be harmful, and that it does not remove odor.

If the consumers of every state had the kind of legislation and enforcement enjoyed by consumers of North Dakota, together with the overall protection afforded by the Federal Food, Drug, and Cosmetic Act, and the Federal Trade Commission control of advertising, and if the Federal Food and Drug Administration had an appropriation of $20,000,000 annually, consumers in the United States would be well protected. That is the goal towards which to aim.

Summary

History has set the precedent, and modern conditions provide the need for legislation to protect consumers of food, drugs, and cosmetics. The Federal Pure Food and Drugs Act of 1906 was inadequate, ineffectively enforced, and outmoded. The first serious effort to rewrite it in 1933 resulted in successful opposition tactics involving compromise and delay. A national tragedy and the fear of businessmen that states would pass rigid laws led to passage of the revised S5 in 1938. A problem of immediate concern is that of financing the expanded operations of the Food and Drug Administration. Unless Congress greatly increases the annual appropriation the new law cannot be enforced effectively. Modern laws have been introduced into the legislatures of several states but our dual form of government renders joint Federal and state control necessary. This will be achieved only when consumers organize effectively and demand adequate laws, supplemented with liberal appropriations for rigid enforcement.

QUESTIONS FOR DISCUSSION

1. Are you subject to any sumptuary laws?
2. Why not let competition regulate the production and sale of food, drugs, and cosmetics?
3. What is the purpose, if any, of the Federal government prosecuting a product as, for example, *U. S.* vs. *19 Quarts of M-E Chlorine Solution?*
4. Would an increased appropriation up to $20,000,000 for the enforcement of the Federal Food, Drug, and Cosmetic law be an extravagance or an investment?
5. In reading this chapter what have you learned about the Federal legislative process?
6. For whose benefit was the Federal Food, Drug, and Cosmetic Act of 1938 passed? Why was it passed in that particular year?
7. What can consumers do to improve the new law? How?

PROBLEMS AND PROJECTS

1. Write a review of *An Autobiography*, by Harvey W. Wiley.

2. Prepare a report on pure food and drug legislation in your state, including a summary of advertising control, and telling how effectively your state laws are enforced.

3. Present a summary of Indiana's or Louisiana's new food, drug, and cosmetic law and of Maine's cosmetic law; see if you can interest your state representatives in similar laws for your state.

4. Summarize the last annual report of the Food and Drug Administration.

5. Let two members of the class debate the question whether advertising should be regulated by the Food and Drug Administration or by the Federal Trade Commission.

6. Write a report on the Sherman Anti-Trust Act as an aid to consumers.

7. Have your library secure a copy of the latest annual report of the North Dakota State Laboratories Department; study the report carefully and write a summary of the kind of protection provided for consumers in North Dakota.

Part Four
CONSUMERS IN A CHANGING ECONOMY

29
Adjusting to New Controls

Consumers in Peace and in War: A Contrast

Purpose of an Economic System. As suggested in Chapter 1, the purpose of a good economic system is to provide an abundance of goods and services efficiently and to distribute them widely among consumers. The purpose of peacetime economic effort is or should be to satisfy as many consumer wants as possible. Although our economic system is not organized to fight wars, we find ourselves involved in armed conflicts from time to time. It then becomes necessary to change our goals. Instead of expecting our economy only to provide goods and services to satisfy consumer wants we expect it to produce the maximum possible amount of war materials for the purpose of winning the war. For the duration of the conflict the satisfaction of consumer wants becomes supplementary to the main purpose of producing goods which will contribute to victory. Modern wars, unlike those of old, cannot be prosecuted as a sideline to a peace economy. Mechanized warfare requires complete use of all possible resources. It is total and all-inclusive in the sense that all citizens of the nation are involved indirectly, if not directly.

The process of converting a peace economy to a war economy involves sweeping changes, most of which are temporary but some of which are permanent. The economies of democracies require far greater changes than do those of Fascist nations. The latter are organized continuously on a war basis whereas the former have always considered peace to be the normal condition and war the abnormal. Consequently, when war does come, even though it may have been anticipated for several years, it requires a sudden and complete conversion of the economic structure. The peacetime economy of a democracy is no better suited to the prosecution of a war than is the family automobile for participation in a 500-mile race at Indianapolis. Efforts to convert both

the economy and the family car to different uses involve waste and inefficiency. Efforts to streamline a car intended for comfortable travel will result at best in a poor racer; likewise, efforts to streamline a peace economy for war purposes results in a less efficient war machine than that of a Fascist nation. Herein lies the secret of the early successes of Germany, Italy, and Japan over countries unprepared for total war. This explains also the growing strength of the war machines of the United Nations, particularly those of Great Britain and the United States.

The nature and the operation of the price system were described briefly in Chapter 1. That explanation holds, however, only for a peace economy. When war comes forces are set in motion which throw the price system out of balance. War materials are in great demand and as a result of temporarily fixed supplies prices tend to rise sharply without drawing forth increased supplies. Moreover, a wartime economy makes use of all resources, one result of which is that some income receivers have larger incomes than in peacetime. In the absence of any restrictions the tendency is to spend their increased incomes. That increased purchasing power in the face of diminishing supplies would result in higher prices. Left to the free play of economic forces the price system in wartime would almost certainly result in unwise allocation and use of resources. It becomes necessary, consequently, to resort to price control and rationing.

In wartime Federal governmental expenditures increase sharply. The government becomes the biggest single consumer. In order to insure supplies of war materials the government stops the production of certain commodities, such as automobiles, so that the production of other commodities, such as jeeps, can be increased. This calls for priorities, which might be described as rationing at the production level. In order to finance its increased war expenditures the Federal government raises taxes and uses its credit by the sale of bonds. To the extent that taxes are raised consumer purchasing power is diminished. And to the extent that bonds are purchased out of savings and income, consumer purchasing power is further diminished. But if the bonds are purchased on credit the total amount of purchasing power is increased with resultant pressure upward on prices. If war expenditures are financed to too great an extent by the sale of bonds the Federal governmental debt is increased and prices tend to rise; both of these results create problems not only during the war but for many years after its conclusion.

At the height of a war effort a modern economy more nearly uses all of its resources than at any other time. In place of unemployment there is a manpower shortage. As a result of the pressing demand for workers many consumers have larger incomes than in peacetime. It is quite

understandable that they wish to use their increased purchasing power but if permitted to do so freely their bidding against one another for diminishing supplies would cause the prices of those commodities, and ultimately of all commodities, to rise. So in a war economy it becomes necessary to allocate resources, to freeze incomes, to ration consumer goods, and to control prices.

But many consumer problems of a peace economy continue in a war economy, and some are aggravated.

Functions and Responsibilities of Consumers in Wartime

Both in peace and in war consumers must perform their three basic jobs. First of these is that of making a choice. Having unlimited wants in the face of limited purchasing power it is necessary for every consumer, having the right of free choice, to choose among the many things he would like to have. Having made a choice, his second job in an exchange economy is that of making purchases in the markets to satisfy his wants. Finally, his third job is that of making intelligent use of his purchases so as to satisfy his wants.

Choosing in Wartime. The analysis in Parts One and Two shows that most consumers perform their three fundamental duties less than expertly. In making their free choices custom, fashion, imitation, and the tendency to show off are institutional and psychological forces which restrict their freedom to choose. These restrictions involve a loss in peacetime, but in wartime they are much more serious. Both for national and for personal interest the thoughtful consumer will reconsider the importance of these forces. For example, customary and habitual consumption of food will give way to rational choices based upon knowledge of nutrition, the limited supply available, and the relative prices of various types of foods. Neither the individual nor the nation can afford the luxury of customary consumption in time of war. For similar reasons the use of many other commodities will be sharply modified or curtailed.

Fashion, imitation, and the desire to keep up with the Joneses should give way to the rigors of war. Thoughtful consumers will wear their clothing longer, perhaps remodeling it more frequently. In other ways patriotic consumers will spend less on conspicuous consumption so that the Federal government can spend more on war materials.

In peacetime market forces such as aggressive selling through advertising and salesmanship, installment selling, and price appeal exert powerful influence on consumer choices. Likewise, such practices as fraud and misrepresentation interfere with consumers' freedom of choice. The latter practices are undesirable both in war and in peace, and some of the aggressive selling practices are peacetime luxuries which can

hardly be afforded in wartime. Thoughtful consumers, for the national and for their personal interest, will seek to free themselves from such forces and practices. In view of the limited supplies of commodities and services they will ignore pleas to buy more or to buy now, knowing that the resources used to make and advertise nonessentials could and should be used to fight the war.

They will resist the lure of installment credit. Instead they will pay off their debts and buy bonds. This is a clear case of putting into practice the recommendation in Chapter 14 that consumers save first and then use their savings for later purchases of durable goods. By thus reversing the process consumers receive interest on their savings instead of paying high rates of interest on their installment credit balances.

Alert consumers concerned with doing their part in promoting the war effort will be more than usually on guard against fraudulent and misrepresentative practices. They will watch the *Monthly Summary* of the work of the Federal Trade Commission, the *Notices of Judgment* of the Food and Drug Administration, the reports of Consumers Union and Consumers' Research, and the bulletins of the Better Business Bureaus.

Buying in Wartime. Some of the preceding chapters have illustrated the hit-or-miss buying practices of some consumers in peacetime. The war has prompted many of them to give greater thought to that important job.

In wartime budgeting is doubly helpful. If expenditures have to be cut, and for almost everyone they do, a budget will facilitate the task. Some or all of the increased tax payments can be met if consumers use a budget to plug the leaks in their expenditures; likewise, budgetary adjustments can be made to permit the allocation of a percentage of income for war bonds. Many consumers will find their real income shrinking, due to rising prices, and will find that a budget helps to meet that problem.

In wartime intelligent buying will pay even bigger dividends than in peacetime. Rising living costs take the form not only of higher prices but also of quality and quantity deterioration. For these reasons the reports of consumer testing agencies such as Consumers Union and Consumers' Research are especially helpful in wartime. Consumers Union issues a weekly publication called *Bread and Butter* which costs only $1 a year. Properly used, it may pay for itself many times over.

There are many Federal government pamphlets which supply useful buying information. There is not room here to give even a representative list, but the individual consumer may write to the Superintendent of Documents, Washington, D. C., for a list of consumer publications. An especially good list is that of the United States Department of Agriculture,

Miscellaneous Publication No. 60. In urban centers many of the pamphlets and bulletins can be secured through Consumer Information Centers. Some of the titles deal with guides for buying sheets, blankets, bath towels, children's clothing, boys' suits, and cotton shirts. One describes how to judge fabric quality. Another series describes the wise buying of food items in wartime such as beef, tomatoes, and eggs. Still another bulletin deals with meat for thrifty meals.[1]

More detailed and orderly treatment of the buying problems of consumers in wartime will be found in four books published since Pearl Harbor. *How to Stretch Your Dollar in Wartime*, by Ruth Brindze, was published by the Macmillan Company, New York, in 1942. *Consumers Can Help Win the War*, by Jessie V. Coles, was published by the University of California Press, Berkeley, in 1943. *Consumers in Wartime: A Guide to Family Economy in the Emergency*, by Leland J. Gordon, was published by Harper & Brothers, New York, 1943. *The Consumer Goes to War: A Guide to Victory on the Home Front*, by Caroline F. Ware, was published by Funk & Wagnalls, New York, 1942.

The careful buyer in wartime will follow the practices described in detail in Chapter 17 and will check his weights and measures as outlined in Chapter 26. He will reconsider the types of stores with which to deal, knowing that he can get the lowest prices only by using all types.

Special Wartime Buying Problems. (1) *Insurance.* Men and women in the armed services find the $10,000 of National Service Life Insurance for which they are eligible to be a good buy. In most cases it would be well to purchase the full $10,000 available, primarily because there are no restrictions on it. Upon discharge from the armed services the National Service Life Insurance should be continued in force and used as the basis of a permanent life insurance program.

Civilians should continue their peacetime life insurance program. If there are any policy loans they should be liquidated if it is at all possible to do so. If the program is incomplete it should be expanded, perhaps more rapidly than originally planned, especially if the insured's income is larger as a result of war employment. For those whose life insurance program is complete and for those who can afford it, it might be well to hedge against depreciation in the capital value of the life insurance estate as a result of rising prices by the purchase of 5- or 10-year term insurance. The cost of living having risen approximately 25 per cent (as of January 1, 1944), the insured would do well to consider adding to a $20,000 life insurance program, $5,000 worth of term insurance. If prices should rise

[1] The bulletins referred to may be identified and secured by requesting the following numbers: *Farmers' Bulletin* No. 1765, No. 1778, No. 1831, No. 1837, No. 1877, No. 1908.

further, proportionate amounts of term insurance could be added to offset the depreciation of the dollar. Another possibility is that of borrowing from a bank at a low rate of interest an amount of money approximately equivalent to the loan value of the insurance, and using the proceeds to purchase investment trust stock which will yield a dividend about equal to the interest on the loan. Then in case of rising prices the principal invested in the stock would reflect the upward movement of prices.

Property owners near the boundary lines of the nation and those near air fields and war plants should protect their investments by the purchase of War Damage Insurance written by the War Damage Corporation, a Federal government agency. It may be purchased through local insurance brokers.

(2) *Housing.* The housing shortage in many war centers with consequent higher rents forces reconsideration of the question whether to own or to rent. Housing shortages are caused not only by increased population in some areas but also by the cessation of normal housing construction for the duration. In reconsidering the question the basic considerations discussed in Chapter 22 must be recognized as applicable in war as well as in peace. It is impossible to escape higher rents by purchasing houses, because the purchase prices tend to reflect the higher rents.[1]

(3) *Investments.* For the typical small investor war involves no major change in savings and investment program. It is important to maintain, perhaps to increase, life insurance. If, as a result of the war, family income is greater, debts should be paid off more rapidly than may be necessary. This applies particularly to mortgages on houses and to installment credit obligations. For the small investor both national and personal interests dictate the purchase of Federal government bonds of the type described in Chapter 23. As part of the broad program of price control it is imperative that everyone allocate a fixed percentage of income to the purchase of government bonds.

Using in Wartime—War on Waste. Both in peace and in war the ultimate purpose of choosing and purchasing commodities is to use them for the satisfaction of our wants. All through the process of choosing and buying there is opportunity for waste, but perhaps the greatest waste occurs in the incomplete and incorrect use of things which have been purchased. For example, the careless and incorrect preparation of foods may result in expensive and unnecessary waste. Discarding clothing

[1] For an elaboration of this point see GORDON, Leland J., *Consumers in Wartime*, pp. 48–60, Harper & Brothers, New York, 1943; rent control is described in the latter part of this chapter.

before it has fully served its purpose, and the wasteful use of fuel, are other points at which careful consumers can economize.

It is important also so to use durable goods as to make them last. This is a matter not only of economy but of necessity. Many household appliances are not being produced in time of war. The Office of Price Administration has issued a series of folders telling consumers how to make household appliances last longer. These cover washing machines, ironing equipment, vacuum cleaners, refrigerators, gas and electric ranges. The production of automobiles was discontinued for the duration so it became imperative to use them carefully and to have them properly serviced. In this connection it is especially important to guard against fraudulent commodities and services. Much damage has been caused, for example, by some wartime anti-freezes, and consumers have wasted much good oil by following the advice of commercial interests urging them to change their motor oil more frequently than necessary.

By the end of 1943 wartime consumers were faced with a serious clothing problem. Low-price clothing was disappearing from city stores, being replaced by more expensive items of lower quality.[1] Careful consumers were using the clothing they had much longer than was their practice in peacetime; by so doing they were helping the war effort as well as themselves.

Governmental Aid to Consumers in Wartime

Consumers Need Help. In peacetime many, perhaps most, consumers fail to perform their functions efficiently or to meet their responsibilities fully. As a result there is much waste. But in wartime the nation cannot afford to let consumers consume as usual any more than it can permit business as usual. If consumers would ration themselves it might not be necessary for the government to do so. But too many consumers place their shortsighted self-interest before their own long-run interests and those of all other consumers in the country. This they do by hoarding, and by failing to conserve the limited supplies of commodities, such as gasoline, rubber, and shoes. Moreover, many wartime economic problems require unity of action which can be achieved only through suspension of the right of free choice. In other words, governments must compel consumers to do certain things and to refrain from doing others. In addition to its many other activities government has to assume the task of protecting consumers from themselves, from the operation of economic forces, and from profiteers. This has been done both by providing information and by compulsory regulation of certain consuming activities.

[1] *New York Times*, December 6, 1943, p. 26; December 8, 1943, p. 28.

Governmental Wartime Aids: Positive. Until May 18, 1940, consumers in the United States were living in a peace economy. On that date the President declared a national defense emergency, since which time American consumers began living in a war economy. Among his many acts for placing the nation on a war basis one of the first taken by the President was that of naming an Advisory Commission to the revived Council of National Defense, which had functioned during World War I. Among the seven commissioners were Harriet Elliott, whose responsibility was to protect consumers, and Leon Henderson, whose responsibility was to stabilize prices. From June, 1940, until April, 1941, the Consumer Division sought to help consumers meet their problems of adjusting to a war economy. It must be remembered that at that time the American economy was operating in second gear. "Reflation" had not reached the goal set by the Administration; consequently the Division took the position that it was possible to have butter as well as guns. A basic plank in its platform was the conviction that in order to make America strong for the days that lay ahead it was essential not only to assist in keeping prices from rising too rapidly but to help raise the plane of living of the submerged one third of the population. The Consumer Division program to accomplish those goals was contained in the following six lines of activity:

(1) "To advise the Commission on consumer needs as they are affected by the defense program and to make recommendations which will balance military and consumer requirements."

(2) "To make sure that the specific problems created for consumers by particular military defense measures are dealt with as effectively as possible." This refers to problems of housing, sanitation, health, recreation, and similar problems which were anticipated in defense areas.

(3) "To promote economic efficiency by contributing to the effective functioning of the price system and by advising on monetary and fiscal matters from the consumer point of view." This portion of the program was concerned particularly with watching the prices of consumer goods and was closely related to Mr. Henderson's major task of price stabilization.

(4) "To promote and co-ordinate positive measures for consumer welfare essential to the total defense program." One of the most important specific problems in this connection was that of nutrition. Agricultural surpluses were still prevalent and one of the aims was to increase food consumption among lower-income groups.

(5) "To consider possible consequences of an intensification of the emergency and prepare preliminary plans for meeting that situation."

(6) "To consider long-range effects of the current defense measures

on public welfare and to anticipate some of the problems of post-emergency readjustment that can be avoided by planning now."[1]

A small staff undertook the Herculean task of helping consumers to meet the pressing problems of an economy which was rapidly being shifted from a peacetime to a wartime basis. Sections of the Division were set up to deal with problems of such groups as labor, Negroes, and farmers. Representatives of the Division undertook to establish co-operative programs with existing organizations in each of those groups and with established consumer organizations. A series of bulletins was published dealing with such topics as *Local Market News Broadcasts for Consumers*, *Check Your Weights and Measures*, *Strengthening the Machinery for Consumer Protection*. For the first time there was compiled a *Directory of Governmental Consumer Services and Agencies*, so that consumer organizations might know those Federal, state, and local agencies which were already performing services for consumers and which might reasonably be expected to expand their activity. An effort was made to secure the establishment of Consumer Information Centers in key localities. It was hoped that through those centers many governmental agencies could co-operate in channeling information to consumers. It was expected also that they might serve as channels of information from consumers to the Consumer Division in Washington, providing a means of recording complaints of price increases.

The program of the Consumer Division never really got under way. There were several reasons. One was inadequate staff and appropriation. Another was lack of positive, aggressive action. The idea of a Consumer Division was strenuously opposed by some business interests. By January, 1941, economic events were moving at such a rapid pace that a plausible case was made out for the combination of the Consumer Division with the Price Stabilization Division, since it was held impossible to draw the line between stabilizing prices at the production and at the consumption levels. In April, 1941, the Advisory Commission was reorganized. The Office of Price Administration and Civilian Supply was established, with the Consumer Division as a subordinate agency. That was the first step in a long period of decline which culminated in the final abolition of the Consumer Division as such. In December, 1941, Miss Elliott resigned, to be followed by short-lived successors. Eventually the Consumer Division became essentially a public relations department of the Office of Price Administration, concerned with educational work dealing with rationing and price control. By the end of 1942 the Division had been rendered practically impotent.

[1] Cassels, John, "The Program of the Consumer Division" in *The Consumer and Defense*, pp. 22–35, edited by Frances Hall, Edwards Brothers, Ann Arbor, 1940.

In the early days of the defense program there were those who thought that the Consumers' Counsel Division of the Department of Agriculture would have been the logical agency to have assumed the task of representing consumer interests. Although it was by-passed, the Consumers' Counsel Division co-operated closely with the Consumer Division of the Advisory Commission from June, 1940, until April, 1941. In September, 1940, for example, the two agencies collaborated in preparing a special issue of *Consumers' Guide*. But the Consumers' Counsel Division was having its own difficulties in the Department of Agriculture, as described in Chapter 27. As a result key personnel was eliminated at the end of 1942 and its effectiveness for consumers reduced to the vanishing point.

The Bureau of Human Nutrition and Home Economics, also described in Chapter 27, directs its energies particularly to the development of a national nutrition program. The results of extensive research are made available to consumers through bulletins, press releases, radio talks, and exhibits. The Bureau played an important part in planning and following up the National Conference on Nutrition for Defense which was held in Washington in May, 1941.

State and municipal consumer aid programs were scattered and incomplete. Efforts were made to co-ordinate the activities of Federal, state, and local agencies but there seemed to be a feeling that the consumer program was too tenuous and that other problems were of greater importance. Under the leadership of the Agricultural Marketing Administration of the United States Department of Agriculture there was some extension of local market news broadcasts for consumers. Under that plan market news is secured from local wholesale and retail markets by market news reporters secured from Municipal Departments of Markets or State Departments of Agriculture or from the Agricultural Marketing Service. That news is assembled, analyzed, and interpreted for consumers by market analysts, home economists, and nutritionists secured from municipal and state agencies. The news is then broadcast over local radio stations. Mention has been made of the Consumer Information Centers, some of which were established in various cities.

Educational programs were undertaken by at least two states. *A Manual of Consumer Education for Wartime Living* was prepared under the auspices of the State Council of Defense of Pennsylvania. Part I deals with materials for teachers and students; Part II with the wartime economic program of the Office of Price Administration; Part III contains consumer units recommended for the junior high school; and Part IV contains the outline of a unit in consumer problems dealing with food, clothing, housing, household equipment, savings, taxation, and

loans. The State Department of Public Instruction of North Carolina, in collaboration with the District Office of Price Administration, prepared a teachers' manual entitled *Ways to Victory on the Home Front.* The bulletin contains unit outlines dealing with consumer wartime problems and contains sources of information and materials. In collaboration with the Office of Price Administration the colleges and universities of North Carolina prepared a bulletin entitled *The Education of Consumers in Wartime.* The limited evidence available suggests that many other educational programs of these types were being developed by state and municipal agencies for the purpose of building a program of wartime consumer education.

Governmental Wartime Aid: Regulatory. In an exchange economy prices serve as a balance wheel. It was well known that in shifting to a wartime basis readjustments would be reflected in the rising prices of some commodities and in the falling prices of others. The crux of the problem was to cushion the adjustment in an effort to prevent extreme and unnecessary price rises. The problem of controlling prices is extremely intricate and may take many forms. Much more is involved than passing a law setting a ceiling on prices. Realization of that fact led the President to charge Mr. Leon Henderson with the task of stabilizing prices. The story of price stabilization efforts and activities down to January, 1944, may be outlined in six stages.

Price Control: First Stage. The first stage was characterized by selective price control. Early activities centered around the control of prices of such raw materials as lead, copper, zinc, and aluminum. Largely through consultation, efforts were made to prevent or to stop speculative excesses. That type of control continued through 1940, but by February, 1941, the danger of a general price rise had become clear. As early as February 17, 1941, an effort was made to peg prices by issuing maximum price schedules whose effectiveness depended upon voluntary co-operation of industry and upon publicity. The refusal of a large automobile company to follow the maximum price schedule for automobiles marked the end of that plan. The next step was to give the Office of Price Administration and Civilian Supply (OPACS) such authority as had been available to the price-fixing committee of the War Industry Board in 1917–1918. That authority, however, carried insufficient penalty provisions to be effective.

Up to April, 1941, the major price control device had been that of increasing the supply of commodities and services. By that time it was clear that bottlenecks were developing in certain lines and that civilian production would have to be curtailed in strategic areas. Yet as national income increased general production increased also, keeping prices from

rising too rapidly. The sales of durable goods, such as automobiles, vacuum cleaners, washing machines, refrigerators, and kitchen ranges, showed increases of 35 to 110 per cent in 1941 over 1939.

On April 16 the first price ceiling was put into effect. Just as the steel industry was about to pass on a wage increase to consumers, OPACS ordered prices on all iron and steel products held at the level prevailing on that date. By the middle of 1941 the slack had been taken out of the economy and it was evident that as consumer demand increased failure of production to keep pace would result in more rapidly rising prices.

The next step was taken on July 30 when the President asked Congress to grant to him authority to establish over-all price ceilings. The House of Representatives started to hold hearings on the proposed legislation August 5 and continued intermittently to September 23, collecting 2,300 pages of testimony. But the Emergency Price Control Bill was not passed until November 28. Nine days later the United States was at war. Yet it was not until January, 1942, that the final Emergency Price Control Act was passed by Congress, being signed by the President on January 30. During those seven months price indexes of uncontrolled commodities had risen from 107 to 125, informally controlled prices had risen from 103 to 108, while controlled prices rose from 98 to 102.

Price Control: Second Stage. The second step of price control was characterized by a partial ceiling on prices. The Emergency Price Control Act of January 30, 1942, created the Office of Price Administration (OPA). Although parity for farm prices had been achieved by October, 1941, the farm bloc had set parity at 110 per cent of the old formula. As a result OPA was prevented from controlling the prices of most agricultural products. General Maximum Price Regulation was issued by OPA April 28, 1942, becoming effective May 11 at the wholesale level, May 18 at the retail level, and July 1 for services. The Regulation set the highest prices charged by each retail store in March, 1942, as an absolute ceiling. When the Regulation went into effect 40 per cent of the average family's food budget was unaffected because farm products were not included. Farm food prices continued to rise at the rate of $3\frac{1}{2}$ per cent a month from May 1 to September 1, causing an alarming increase in the cost of living.

Coincidental with General Maximum Price Regulation, rent control was inaugurated on April 28, 1942, in 302 defense areas in 46 states. In most cases rents were frozen at the March 1, 1942, level but in cases where they had risen exorbitantly they were cut back to July or April or even to January, 1941. As of June 30, 1943, 456 defense rental areas had been designated, of which 368 with an estimated civilian population of 78,600,000 had been placed under Federal rent control. It is estimated

that for 1943 savings to renters amounted to $1,000,000,000, but those savings were not made at the expense of property owners. An OPA survey revealed that due to high and increasing occupancy and stable or sluggish expenses owners of rental housing property were in a more favorable operating position than in the prewar years. Rental income for the average apartment house unit in the sample rose from $482 for 1939–1940 to $542 in 1942. Total expenses remained relatively stable, increasing from $302 to $305. As a result net operating income increased more than 31 per cent from $180 in 1939 to $237 in 1942. A similar situation was found for smaller structures. Rental income rose from $365 in 1939 to $407 in 1942. During the same period expenses declined from $227 for the average unit to $206, resulting in an increased net rental income of 45 per cent.[1]

Extension of installment credit was placed under control in August, 1941. The volume of consumer short-term debt had risen to a new high point of $9,700,000,000, which was approximately $1,000,000,000 more than in 1940. If allowed to continue at that rate installment credit would have become a serious inflationary factor. The first controls were placed on credit purchases of automobiles, washing machines, ironers, and vacuum cleaners. In March, 1942, coincidental with rent and price control, installment credit controls were extended and stiffened. As a result the outstanding short-term consumer debt was reduced to $8,300,000,000 by April, 1942. Nevertheless, controls were extended further in May, 1942. Installment borrowing restrictions were made more drastic and the list of articles covered was extended to include practically all things purchased on time payment plans or charge accounts. Under the new regulations a down payment of at least one third of the purchase price was required, the balance to be paid in 12 months. There were a few exceptions such as rationed automobiles, the payment for which might be spread over 15 months, and for furniture and pianos, the required down payment of which was 20 per cent; property lost or damaged in a flood could be replaced without restrictions; furnaces could be converted from oil to coal and houses could be insulated. Installment payments had to be not less than $5 a month or $1.25 a week. Charge accounts had to be paid or put on an installment basis by the tenth of the second month following the month in which the purchase was made; otherwise, the account had to be closed for further credit. To avoid evasion of installment credit controls the Board of

[1] The factual data for the foregoing and for the following discussion of price control are drawn chiefly from the first six *Quarterly Reports* of the Office of Price Administration, which cover the period down to June 30, 1943. A supplementary source of information is *Battle Stations for All: The Story of the Fight to Control Living Costs*, issued by the Office of War Information, February, 1943.

Governors of the Federal Reserve System also limited personal loans to 90 days. Even then they could be secured only after filling out a form requiring detailed information as to the purpose of a loan. As a result of the increased restrictions the outstanding value of consumer short term debt had been reduced to $6,500,000,000 by September, 1942.[1]

Price Control: Third Stage. The third stage of price control was characterized by over-all price ceilings. The reader will recall that the Emergency Price Control Act of January 30, 1942, covered only about 60 per cent of the food items in the cost of living index. There were many other exceptions in General Maximum Price Regulation also. As a result prices continued to rise. On April 27, 1942, the President delivered his seven-point anti-inflation program which called for price ceilings, rationing, farm price stabilization, wage stabilization, the reduction of credit purchases, heavy taxation, and the purchase of war bonds. Six months passed with no action by Congress. During that period basic inflationary factors were at work. There was an increase in the number of individual breaks in price ceilings, attributed to conditions resulting from uncontrolled farm prices and uncontrolled wages. On September 7, the President intervened with a fighting speech in which he declared that if Congress did not increase the powers of the Price Administrator he would use such war powers as were available to him. Finally on October 2 Congress amended the Emergency Price Control Act in accordance with the President's recommendations. The next day the Office of Economic Stabilization was created. Two days later OPA froze the prices of poultry, butter, cheese, and similar items, bringing up to 90 per cent the proportion of all food prices under control at retail, in contrast to the 60 per cent previously under control.

During that period the rationing program was made general. Previously rubber, fuel oil, gasoline, sugar, coffee, automobiles, and typewriters had been rationed but it was not until February, 1943, that the general food rationing program was established. There are several reasons why food rationing became necessary in 1943. As a result of increased incomes consumer demand for food products had increased. For example, in the year 1941–42 civilian consumption of canned vegetables increased 33.5 per cent over the annual civilian consumption for the period 1936–39; likewise, annual civilian consumption of canned fruit increased 36 per cent. Another factor was the increase in size of the armed forces, whose food consumption was much greater than that of civilians. The War Department estimates that a soldier eats twice as much as a civilian. Also for the first time in their lives many soldiers were

[1] *Battle Stations for All*, p. 57; Board of Governors of the Federal Reserve System, *Consumer Credit: Regulation W.*

getting as much food as they should have and such luxury items as butter. Still another reason was the increasing volume of Lend-Lease shipments to the United Nations.

Shoe rationing was instituted February 7, 1943. The need for that action was based upon a potential demand for 476,000,000 pairs of shoes as against a possible production of 330,000,000 pairs. That scarcity likewise was caused by increasing military demands, the requirements of Lend-Lease, and the reduction of leather imports.

It may be assumed that all consumers reading these pages are familiar at least in a general way with the coupon system of point rationing. Having received his allotment of points, each consumer was then required to give up a specific number of points as he bought various food items. The retail merchant in turn was required to surrender coupons in order to replenish his stock. It would be manifestly impossible to count the millions of coupons turned in by retail stores, yet it was necessary to check on them as a means of enforcing the program. Consequently OPA developed a system of counting ration stamps by weight. That was successful at first with a margin of error of only 2 per cent. But retailers proceeded to stuff envelopes with blank pieces of paper. That practice reached such proportions that in one week there was a deficit of 13,000,000 points in Boston alone. To check such frauds OPA devised a new scheme effective February 27, 1944, under which all coupons were given a uniform point value of ten, and tokens were used for change.[1]

It is imperative for consumers to understand clearly that they share responsibility for the success or the failure of the price control and the rationing programs. If there are "black market" operations it is because some consumers are buying outside the established channels of marketing. It takes both a buyer and a seller to violate the price control and the rationing programs. If every consumer would pledge himself to purchase only those commodities allotted to him under the rationing program and to pay only the ceiling prices, price control and rationing would work and there would be enough of all commodities for everybody at steady prices.

But there are always those who will avoid or evade the rules of the game. Consequently it was necessary for OPA to enforce the program as effectively as it could. Unfortunately its appropriation was too small to provide the necessary personnel for adequate enforcement. For the fiscal year ending June 30, 1943, it was estimated that the rationing program cost 50 cents per capita for the administration of 13 separate programs. Expressed in another way, this means that rationing cost less than 4 cents per person per program for the year. This was a very small

[1] *New York Times,* January 25, 1944.

price to pay for the assurance that everyone would get at least one serving at a fair price before anyone got two or more.[1]

Price Control: Fourth Stage. The fourth stage of price control was characterized by the change to community price ceilings. Throughout 1943 price ceilings had been based on the original formula of General Maximum Price Regulation which set as the ceiling price in each store the highest price charged in March, 1942. During the first quarter of 1943 that plan was abandoned in favor of dollars and cents ceilings on a community-wide basis. The reason given by OPA for making the change was that the new ceiling formula would facilitate administration. It was argued that there was no effective way for consumers or OPA enforcement officers to check the validity of the March 1942 prices of individual stores. On the other hand, it was claimed that if ceilings were established and expressed in terms of dollars and cents and were identical on a community-wide basis it would be possible for consumers to compare and to check the compliance of retail merchants. The new community prices were calculated on the basis of cost data in each community, to which were applied the allowable wholesale and retail markups. Net cost plus markup equaled the ceiling price. Retail stores were divided into four groups according to the annual volume of business and according to type. Class I stores were independents whose volume in 1942 was less than $50,000; Class II were independents with a volume of $50,000 to $250,000; Class III included chain stores having a volume up to $250,000; Class IV included all stores whose sales exceeded $250,000 in 1942. To illustrate the operation of the new plan here are a few random ceiling prices in the New York area as of November, 1943: a 20-ounce package of Aunt Jemima Pancake Flour was priced at 13 cents in Group III stores and 12 cents in Group IV; a 44-ounce package of Swansdown Cake Flour had a ceiling of 28 cents in Group III stores, compared with a ceiling of 26 cents in Group IV stores; a quarter-pound package of Lipton's tea was priced at 27 cents in Group I stores and 26 cents in Group II stores. Generally speaking there was much less disparity in the ceiling prices between stores in Groups I and II than between stores in Groups III and IV. This also means that there was considerable disparity on most items between stores in Group I and those in Group IV. In this connection the reader should turn back to page 238 in Chapter 13, where Table XIII indicates community price differences among the various classes of stores.

In addition to the allowable markup, retailers were permitted to include a specific charge for delivery services. They were permitted to

[1] *Battle Stations for All*, Chap. 11, p. 24; Office of Price Administration, *Fifth Quarterly Report*, pp. 17, 30; *Sixth Quarterly Report*, pp. 13, 18.

charge 10 cents for purchases ranging from \$2 to \$2.99; 15 cents for purchases ranging from \$3 to \$4.49; 20 cents for purchases ranging from \$4.50 to \$5.49; and 25 cents for purchases ranging from \$5.50 up.

By the end of June, 1943, community prices had been established for approximately 1,000 grocery items in 200 major cities. By the end of the year the number was much larger since the plan went into effect for dry groceries on August 5, 1943.[1]

Perhaps the most significant feature of the community price ceiling program is the fact that it was based on brands, largely those which were nationally advertised. Consequently the ones who really gained then and in the long run were the national advertisers. At a time when food supplies were limited and advertising them was unnecessary the national advertiser was nevertheless encouraged by this price policy not only to continue but to expand his advertising program. The net result was that the community ceiling price program was an official recognition of and free publicity for nationally advertised brands. There was no provision, at least none effective, permitting consumers to purchase food items in bulk. Whether or not consumers gained under the community price ceilings there can be no doubt that producers, distributors, and advertisers of branded merchandise made very significant gains.

The fourth stage in price control might be characterized further as that in which Congress openly opposed effective price control. From the very beginning there was a group in Congress which, if it did not oppose price control, certainly did not support it. That was indicated by the failure to include farm prices in the first Emergency Price Control Act. It was only under the most vigorous executive leadership that Congress amended that Act. In the meantime the Price Administrator had performed an effective job of organization, administration, and enforcement. The record shows that prices included under the Act stopped rising while those not included continued to rise at an accelerating rate. As OPA expanded, personnel and public relations problems multiplied. The record shows that OPA followed the standard procedure of the Civil Service Commission in recruiting personnel. The test for appointment was ability to do the job rather than party regularity. Congressmen began to complain that they were not consulted about appointments in their areas. Democrats objected to the appointment of Republicans and Republicans objected to the appointment of Democrats. Before he realized it the Administrator was in the midst of a patronage fight. Doubtless there were other factors involved but by the summer of 1942 it was evident that Leon Henderson was on the way out.

[1] Office of Price Administration, *Fifth Quarterly Report*, pp. 2–3; *Sixth Quarterly Report*, p. 2; *Retailer's Bulletin No. 36*, July, 1943.

A Congressional bloc made it clear to the President that unless Henderson was replaced as Administrator there would be no appropriation for OPA.

The decision was made in dark December of 1942, and with a shift in personnel came a shift in policy. The newly appointed Administrator, former Senator Prentiss W. Brown, assumed the task of appeasing a Congressional bloc which had discovered its power. The outcome was evident from the very beginning. Mr. Brown found himself in the midst of a hopeless cross-current in which appeasement was not enough; the price of Congressional favor was practically complete capitulation. Those in Congress who did not want effective price control began to attack the personnel of OPA from the Administrator on down the line. There is not room here to describe the devious tactics which were used, but the outcome was complete surrender to the Congressional demand that OPA be turned over to "practical" businessmen. Mr. Chester Bowles, an advertising executive, was appointed Administrator in October, 1943. Earlier Congress had attached a rider to an appropriation bill requiring that all OPA policy-making personnel must have had five years "practical" business experience immediately prior to appointment. But Mr. Bowles and his fellow businessmen have learned what his predecessors learned—that there is an inflationary bloc in Congress. That group wants the appearance of price control without its reality. Chief among the inflationary group are the farm representatives. This is to be explained by the fact that farmers stand to gain by inflation in two ways: farmers are businessmen whose income takes the form of profit; as prices of farm products rise farm income rises more rapidly than do farm living costs. The second reason is that most farmers are in debt and debtors always favor rising prices for it is thereby easier to pay off loans.

All this shows that in addition to having a law and an appropriation for enforcement there must be a will to enforce. If the Administrator has that will Congress may insist upon his replacement by someone presumably amenable to Congressional wishes. In the fiscal year 1943–44 the farm bloc and the patronage group were in control and were getting what they wanted. This is another way of saying that consumers were not getting the kind of price control they should have had.

The questions of standards and grade labeling are involved in Congressional opposition to effective price control. At the outset of the price control program it was recognized by all those familiar with the problem that it is impossible to control prices without controlling quantity and quality. Without quality controls indirect price increases may take many forms. The wool content of woolen fabrics may be reduced; thread

counts in cotton fabrics may be reduced; rayon and cotton may be substituted for silk; cheaper grades of leather may be substituted for better grades in shoes. A common form of indirect price increase is to eliminate cheaper lines; men's $1 shirts were no longer offered by 1943; women's $2 shoes were discontinued; laundry and cleaning establishments generally discontinued the cheaper types of services formerly available. Still another device was to discontinue a former product for which a "new" product was substituted at a higher price. Contrasting two pairs of shoes made by the same manufacturer and sold by him under the same style number at the same price, it was found that the 1943 pair would give 30 per cent less wear than those made in 1941; hence at the same price in 1943 as in 1941 there was an indirect price increase of 42 per cent.[1]

Price increases may take the form also of concealed or partially concealed reductions in weight, measure, or content. Knowing how few consumers check the net weight or measure of the things they buy, weights and measures officials have found that in peacetime many manufacturers can increase prices by the simple device of reducing the quantity delivered. When the new net content is carried on the label there is nothing illegal and consequently no one to protect the careless consumer from himself. Under the Emergency Price Control Act, however, one of the prohibited acts was that of diminishing the net weight, measure, or content of a commodity while continuing to sell it at the same price. Consequently the main omission in the Emergency Price Control Act proved to be failure to tie prices to quality. OPA officials were confident that there was implied authority in the Act to permit them to establish standards against which to measure the quality and the price of commodities. Consequently a program of standardization was inaugurated in the early days of OPA. By the middle of 1943 there were 250 price regulations which set ceiling prices on the basis of standards. Most of the standards—161—were those already well established in the trade; 5 were in use by other Federal government agencies; 27 were in use in the trade or were required by another government agency; and 57 were established by OPA. With the issuance of Maximum Price Regulation 339 requiring grade labels for hosiery, a storm of opposition broke loose. Congressional opponents conducted hearings in which all those who were opposed to standards and grade labeling were encouraged to testify, but as of January, 1944, no proponent had been permitted to appear before the Committee.[2]

[1] Ulmer, Melville J., "Indirect Price Increases," in *Monthly Labor Review*, vol. 55, pp. 903–912; *CIO News*, December 27, 1943.

[2] *Brand Names and Newsprint, Hearings* before a Sub-Committee of the Committee on Interstate and Foreign Commerce, House of Representatives, Seventy-Eighth

At the same time OPA ordered the 1943 pack of canned goods to carry grade labels using the letters A, B, C, D, to designate the quality of the contents of the cans. The Canners' Association had fought successfully under the NRA to forestall a similar requirement, and later had prevented inclusion of such a provision in the Federal Food, Drug, and Cosmetic Act of 1938. Joining hands with hosiery manufactuers, the two groups moved from OPA up to Capitol Hill to secure relief from the OPA order. The lobby succeeded in securing a Congressional resolution authorizing an investigation of the standards program of OPA. The partial character of the hearings on brand names has been indicated. Not one consumer representative was heard by the Committee. The net result of the hearings was a Congressional amendment to the Commodity Credit Corporation Act which specifically prohibited OPA from requiring standards and grade labeling.

In spite of the boost given to brands under the community price ceiling program, manufacturers and canners asserted that OPA's program of including quality control with price control would ruin brand names, free private enterprise, and advertising. These views were expressed in the words of two witnesses one of whom testified, "I honestly feel that this Maximum Price Regulation 339 requiring grade labeling of hosiery is the worst blow that has ever been struck against free enterprise in the entire history of this country. It is diabolical and it is malicious. It is a deliberate attempt to change business practices and reform industry under the guise of a war necessity."[1] The Secretary of the Association of National Advertisers said, " . . . if grade labeling goes through . . . national advertising by manufacturers is going to fold up. It will reduce the amount of advertising very heavily, because there is only one place to get money for advertising, which is margin; and if margin is eliminated, there is no advertising. . . . "[2] A much less emotional conclusion based upon a survey of 270 housewives in various economic groups in Lawrence, Kansas, is that while grade labeling will not help the well-established brands it will benefit the less well-known brands of merchandise. Moreover, grade labeling will not replace brands but it will materially increase price competition if it is widely adopted.[3]

Congress, Part I, May and June, 1943; Part II, June, 1943. The one exception was the surprise appearance of Honorable Chet Holifield, member of Congress from California. On the basis of his business experience he supported the use of standards and grade labels by OPA; see pp. 373–393, Part I.

[1] *Brand Names and Newsprint*, p. 225, Part I. [2] *Ibid.*, p. 207.

[3] KEBKER, B., "Will Grade Labelling Pay?" in *Journal of Marketing*, pp. 185–188, October, 1943.

Space does not permit further analysis of the arguments for and against the use of standards and grade labeling; this is not necessary, however, since the question was discussed in Chapter 25 and the basic issues were the same in this controversy as in earlier ones. The record shows that opponents of grade labeling and effective price control, led by the Canners' Association, were successful once more in their determination to keep consumers from getting dependable, factual information concerning the quality of the merchandise they buy. The immediate result of course was further to weaken an already tottering price control program.

Advertising in a War Economy. Prominent in the fight against tying price control to standards and grade labels were advertisers in general and national advertisers in particular. Perhaps no further comment is needed as to the reasons for their opposition than to recall the statement of the Secretary of the Association of National Advertisers. This raises the question as to the proper function and extent of advertising in a war economy. Consideration of this question will be brief in view of the fact that two entire chapters have already been devoted to the analysis of the role of advertising in a peace economy. In a nation at war faced with shortages of food, clothing, and practically all essential materials including newsprint, it might be supposed that the general program of restricted output and rationing applied to other commodities and services would be applied to advertising. Logic would dictate the conclusion that if items cannot be obtained or can be obtained only in limited quantities far below the demand for them there is certainly little if any need to create consumer demand. The scarcity of newsprint would likewise seem to dictate a sharp reduction in the use of paper for advertising unavailable goods or nonessentials. Finally the manpower shortage would seem to require the use of large numbers of printers, artists, and others affiliated with the advertising industry in occupations more directly concerned with prosecution of the war. This is not to deny the effectiveness of the use of advertising for war purposes as used by the government in the sale of bonds nor the proper use of advertising for other legitimate purposes.

The record shows that the volume of advertising actually increased during the war. Following a temporary and rather sharp decline during the first four months of 1942, the volume of advertising reached its prewar level later that year, with the *Tide* advertising index at 120. Following two short and small declines, the volume of advertising increased sharply at the beginning of March, 1943, to a peak of 160 in September. From that point it declined to 140 in December, recovered to 150 by February, 1944, and fell to 135.5 by March, 1944. The index shows that

every type of advertising media showed an increase in March, 1944, over March, 1943, ranging from 4 to 38 per cent.[1]

Every suggestion that the volume of advertising should be brought under control has been vigorously and bitterly opposed by advertisers. Many apparent reasons are given but the real reasons are to be found in the determination of manufacturers to keep their brand names in the public consciousness[2] and the determination of advertising and publishing interests to continue their profitable enterprises unhampered. Another reason is that advertising costs are permissible deductions in figuring net income before taxes, which means that the larger the advertising outlay of a firm the smaller its net revenue for income tax purposes.[3] In effect the Treasury policy in 1942–44 was a subsidy to advertising. Yet all proposals that the Treasury lower the advertising allowances deductible for tax purposes have been ignored. In December, 1942, two hundred nine college professors signed an open letter to the Secretary of the Treasury, the Director of Economic Stabilization, the Chairman of the War Production Board, and the Administrator of the Office of Price Administration, expressing the following four convictions: (1) There is little need to stimulate current consumption in wartime, and advertising which seeks to do so is inflationary; (2) the continuation of the full peacetime volume of advertising involves waste of scarce raw materials, power, transportation, and skilled labor; (3) the Treasury should permit commercial companies to deduct for tax purposes only that advertising expense which is necessary to secure the sale of the actual current output; (4) the government should pay for its own advertising directly. The letter was ignored, publicly at least, by the four officials to whom it was addressed. Among the advertising trade press an amazing volume of reaction occurred ranging from rationalization to extreme emotion. There were a few in the advertising fraternity who were courageous enough to express their agreement with all or some of the points made by the professors, but in general the opposition was overwhelming.[4]

The only official body to raise a question about the volume of advertising in wartime was the Truman Committee Investigating the National Defense Program. In its report on two firms the Committee said, "The bulk of the cost of such advertising will be borne by the Federal Government because it has been treated as an expense of doing business before computing profit on which the Government would be entitled to receive

[1] *Tide*, May 1, 1944, p. 107.

[2] Scott, James B., "Advertising When Consumers Cannot Buy," in *Harvard Business Review*, Winter 1942, p. 207.

[3] See editorial comment in *Printers' Ink*, January 28, 1944, p. 10.

[4] *Printers' Ink*, January 8, 15, 29, 1943; February 19, April 30, 1943; *Advertising Age*, March 15, 1943; *Tide*, January 1, 1943; *Editor and Publisher*, December 26, 1942.

excess-profit taxes at the highest rates. . . . " In a personal statement Senator Truman expressed the conviction that "the Bureau of Internal Revenue should investigate these advertising costs and determine the amount the government is entitled to receive as income taxes. The agencies in charge of renegotiation should also investigate and determine the amount to return as excessive profits."[1] But as of January 1, 1944, no action had been taken.

As the paper shortage became more critical it was met, not by reduction of advertising, but by the reduction of editorial content. Of 21 leading magazines surveyed all but one carried more advertising pages in 1943 than in 1942. In one case advertising space was increased by 54 per cent.[2]

By contrast, Australia early placed advertising under control. The order limited certain advertisers to six specific methods and restricted the amount of copy and art work all as a part of the program of rationing and conservation of manpower, paper, and printing materials. Unillustrated posters, showcards, and window stickers might be used in shops actually selling the goods advertised. Advertisements in newspapers, periodicals, and magazines had to limit their subject matter to the name and address of the firm, an established slogan, and a statement that specified rationed goods were available and their price. Also permitted were the trade names or trademarks of rationed goods and a description of how to use them economically and how to prolong the life of a product. Advertisements on billboards when the order was issued were permitted to remain but they could not be repaired, renewed, or replaced. There are numerous other features of the regulation, all of which add up to a sharp restriction in the use of advertising in Australia's war economy.[3]

Price Control: Fifth Stage. The fifth stage may be characterized as the period in which an effort was made to "hold the line." Immediately after the attack on Pearl Harbor leaders of organized labor voluntarily gave their pledge that there would be no work stoppages during the war. In return they were promised by the Administration that their rights of collective bargaining would be preserved and the National War Labor Board was established for that purpose. Representatives of organized labor were assured also when wages were "stabilized" that the rest of the Administration program would be executed so as to prevent any price increases and excessive profits. The story of the effort to get price control legislation has already been told. During the delay prices con-

[1] *Tide*, August 1, 1943; October 1, 1943.
[2] *Tide*, October 1, 1943.
[3] United States Department of Commerce, Bureau of Foreign and Domestic Commerce, *Advertising and Its Role in War and Peace*, Industrial Series No. 5, United States Government Printing Office, Washington, 1943.

tinued to rise and after the first price control act was passed prices of uncontrolled food products continued to rise. These price increases continued until the cost of living index prepared by the United States Bureau of Labor Statistics showed a 15 per cent increase. Quite understandably organized labor was becoming very restive and it was made clear to the Administration that unless the line were held on prices it would be impossible to restrain outbreaks of work stoppages. Consequently the National War Labor Board in September, 1942, adopted the "Little Steel" formula. Under that formula all workers whose wages had not increased by 15 per cent above the January 1, 1941, level were to be allowed a 15 per cent increase. All requests for increases above that amount were to be denied. Assurance was given that taxes would be increased, profits reduced, and other inflationary factors placed under control. In short, the "Little Steel" formula established a new line which was to be held against further increases in the cost of living.

But prices kept on rising. It was simple enough for those charged with the responsibility of controlling prices to point to the causes for the continued rise, but owing to the Congressional situation it was practically impossible to counteract the trend. As suggested in previous paragraphs there were those who wanted only the appearance of price control, which meant that the numerically larger but politically weaker number who wanted real price control got shadow instead of substance. The cost of living index gradually crept from 115 up to 120 and then began to move towards 125.

Again representatives of organized labor made it clear that since the Administration had failed to keep its promise to hold the line they felt that they were relieved of their promise not to strike. The situation was very serious and demanded drastic remedial action. The proposed remedy took the form of a suggestion that by the use of subsidy payments to producers the cost of living would be rolled back; that is, reduced to the level of 115 per cent where it stood as of September, 1942. OPA undertook to reduce the retail prices of meat and butter 10 per cent. The program was announced May 7, 1943, and plans were made to finance it with funds obtained from the Defense Supplies Corporation, a subsidiary of the Reconstruction Finance Corporation. Price reductions of 50 per cent were announced for cabbage and 25 per cent for lettuce. It was argued that the use of comparatively small sums for subsidy payments would save billions of dollars for consumers and for the Federal government. In the case of apples alone it was estimated that the roll-back program would save $20,000,000 to $30,000,000. The reasons for this are to be found in the differences in producers' costs. For example, if it costs one group of producers $5 a bushel to raise apples,

a second group $4.90 a bushel, a third group $4.80 a bushel, a fourth group $4.70, and a fifth group $4.60, the net result of letting the market price of apples rise to $5.10 a bushel is to give low cost producers a windfall profit. Under the subsidy plan the price of apples would be rolled back to $4.80 and producers in groups one and two would be paid a subsidy of 20 cents and 10 cents per bushel on their entire crop, whereas producers in groups three, four, and five would not receive the additional sum. Obviously the cost of subsidizing a portion of the apple crop would be much less than paying 10 cents per bushel more on the entire crop. Applied to fresh fruits, vegetables, meats, and other selected products whose prices had risen excessively, the cost in 1943 was approximately $800,000,000. Estimates of the savings purchased by the subsidy program were as high as $2,500,000,000.

As a result of the subsidy program the rise in the cost of living, which had proceeded without interruption from the early months of 1941, was brought to an abrupt halt. In June, July, and August, 1943, the cost of living index fell a fraction of one per cent each month. In September, 1943, it turned upward again.[1]

In order to continue the subsidy program the Administration had to secure the approval of Congress and the appropriation of funds. In spite of the fact that the record in the United Kingdom and Canada and our own limited experience showed the effectiveness of subsidies in controlling the cost of living there were those in Congress who attacked the program vigorously and bitterly. Justifiable opposition was raised against the so-called flat subsidy which would reimburse apple growers in all groups, including four and five. In the course of the debate much heat was generated and much confusion created in the public mind. By the end of 1943 it became quite apparent that those opposed to the subsidy program were those same ones who had consistently opposed price control. Strong groups lined up on both sides of the issue with the result that those who wanted subsidy support were not strong enough to carry it while those who opposed it were not quite strong enough to kill it. As Congress adjourned at the end of 1943 a compromise resolution continued the subsidy program temporarily until February, 1944.

In the meantime the cost of living index has begun to rise again. Representatives of organized labor then served notice that they no longer felt bound to abide by the "Little Steel" formula and undertook actively to seek wage increases to bring them in line with the increased costs of living. It has been estimated that a 10 per cent increase in wages would in itself increase the cost of living by 4½ per cent. In absolute figures that

[1] See President's Food Message to Congress, November 1, 1943, in *New York Times*, November 2, 1943.

would increase the cost of the war annually by $4,500,000,000 and the cost of living for the nation's consumers by an indeterminate amount.[1] If prices are not held by subsidies it was estimated that in 1944 the cost of living would go up at the rate of 1 per cent per month and that the increase would accelerate as it continued.

That was the picture as of January, 1944. The outlook for effective price control was very dubious, not because we do not know how to control prices, but because Congress failed to enact the necessary legislation and to appropriate the necessary funds. Failure to hold the price line in 1944 would certainly affect the well-being of American consumers for years to come.

Price Control: Sixth Stage. The sixth stage of price control may best be characterized by the phrase "breaking the line." Expressed in positive language this means that the stage had then been reached where one heard and read more about "controlled inflation" than about price control. While Congress broke the line of price control by failing to support the subsidy program, the standards program, and the grade labeling plan for quality control, the business-minded policy makers in OPA continued to search for formulas which would hold prices without hurting anybody. Finding it impossible to devise such a formula the trend seemed to be to find a formula which *appeared* to control prices and which would please everyone in the trade. Even this assignment was difficult, and as of January, 1944, no one had succeeded in discovering such a formula. In the food division there was much talk of "floating ceilings" and "formula pricing." Canners like "formula pricing" because it is simple and eliminates the need for grade labeling. But critics claim that it permits large markups by the packer. "Floating ceilings" would permit retailers to readjust prices at frequent intervals on the basis of shifting costs and it is charged would completely destroy community price ceilings and make enforcement impossible.

In such retail lines as hardware, shoes, dry goods, furniture, drugs, and variety goods, there was talk of a new pricing plan which would place such items in three classifications. Goods in class 1 would be covered by a flat price; the retailer of those in class 2 could mark up the price according to his traditional practice; while items in class 3 would be controlled only indirectly through the requirement that total store markups, including the markup on classes 1 and 2, shall not exceed the over-all markup for a specified period such as possibly the year 1940.

[1] See President's message vetoing the Commodity Credit Corporation bill because of its anti-subsidy clause, *New York Times*, July 3, 1943; also statements by Price Administrator Chester Bowles before the Grocery Manufacturers Association in New York, *New York Times*, November 6, 1943.

Even the trade did not understand the plans or approve them. Discussion in the trade journals was reminiscent of the days of NRA when industry groups, given a free hand to write their codes, quarreled among themselves for positions of relative advantage.

Price Administrator Chester Bowles was reported as being disillusioned and discouraged. In a press conference late in 1943 he was reported to have said that he had been naïve enough to believe that if he brought in good men and did an honest job he would get support for price control. With some bitterness he had concluded that many critics did not want prices controlled.[1]

Price Control: Evaluation. Although our control of prices has been incomplete it has been effective where applied, as shown in Table LXI:

TABLE XLI.—CHANGES IN THE COST OF LIVING[2]

May 15 to September 15, 1942

All items	+ 1.6	Clothing	−0.3
Controlled	− 0.3	Rents	−1.7
Uncontrolled	+ 4.7	Fuel, electricity, ice	+1.2
Food	+ 4.1	House furnishings	+1.1
Controlled	+ 0.2	Miscellaneous	+0.5
Uncontrolled	+10.2		

Compared with price control in World War I, price control in World War II has been much more effective. In the first 43 months between the outbreak of war in August, 1939, and March, 1943, wholesale prices rose 38 per cent; during the first 43 months of World War I wholesale prices rose 82 per cent. During the first 43 months of World War II the cost of living rose 25 per cent; during the first 43 months of World War I the cost of living rose 41 per cent. At the peak of inflation during World War I the cost of living rose at the rate of 2.8 per cent monthly while food prices rose at the rate of 4.4 per cent monthly. From 1914 to June, 1920, the cost of living more than doubled; as a result the 1914 dollar had a purchasing power of 48 cents in 1920. In World War I military expenditures totaled $31,000,000,000 but of that amount $13,500,000,000 represented unnecessary price rises. Interpolating on the basis of those figures, unnecessary price increases in World War II might easily cost as much as $100,000,000,000.[3] It is estimated that General Maximum Price Regulation which went into effect in May, 1942, saved the average family $12.89 on clothing, $7.54 on meat, and $3.40 on other foods in the year May, 1942, to May, 1943. The estimate is based on the fact that prior to price control prices had been rising at

[1] *Advertising Age*, December 13, 1943; *New York Times*, November 7, 21, 1943.

[2] Office of Price Administration, *A Manual of Price Control*, p. 302, United States Government Printing Office, Washington, 1943.

[3] *Battle Stations for All*, p. 14; *A Manual of Price Control*, p. 302.

the rate of 1 per cent a month, whereas price control reduced the rate to $\frac{1}{2}$ per cent a month. The ceiling price on cigarettes alone is estimated to have saved smokers $142,000,000 annually.[1]

Comparing price control in the United States with that in Britain and Canada, it is found that we have done better than the British though not quite as well as the Canadians. By March, 1943, wholesale prices in the United States had risen 38 per cent above the level of August, 1939; in Canada they had risen 36 per cent, and in Great Britain 65 per cent. During the same period the cost of living increased 25 per cent in the United States, 16 per cent in Canada, and 28 per cent in Great Britain. Since that time, however, price control in the United States began to slip so that the cost of living was rising again, whereas the British had held their cost of living steady for more than two years.[2]

The foregoing evidence fortifies the conclusion that prices can be controlled effectively if we have a will to do so. Until 1944 the record in the United States was really better than we deserved, but if the line was not held the position thus far defended against inflationary attacks would have to be abandoned.

Price Control: Enforcement. The Emergency Price Control Act carried the following enforcement authority: any person who willfully violated any provision of Section IV and any person who made any statement or entry false in any *material* respect was subject upon conviction to a fine of not more than $5,000 or to imprisonment for not more than three years in the case of a violation of Section IV and for not more than one year in all other cases.

It was provided further that any consumer buyer might sue any seller who violated a maximum price schedule. He could sue for $50 or treble the amount by which the price paid exceeded the maximum price, whichever was greater, plus attorney's fees and costs. It was hoped and expected that the latter provision would enlist a large army of buyers in the enforcement corps. Although this provision was upheld at first, in subsequent cases the courts construed the Act to mean that the complainant was entitled only to the amount by which the price paid exceeded the ceiling price.

In the early days of OPA the Administrator was reported to have said that it would have taken an army of 80,000 price investigators adequately to enforce price control. A proposal to enlist housewives as volunteer shoppers was announced in April, 1942, but for reasons which are obscure was never effectuated. By the end of June, 1943, the price panel plan had been established in 4,700 of the 5,500 local war price and rationing

[1] *Battle Stations for All*, p. 8.

[2] *A Manual of Price Control*, p. 302.

boards. It was estimated that 20,000 volunteer members were working on price problems with an additional 25,000 price panel volunteer assistants.[1]

The power of OPA to enforce quality control was denied by Congress. The power to enforce quantity control was contained in the Act but was contested in the courts. A United States District Court refused to enjoin a candy manufacturer from selling a five-cent bar the weight of which had been reduced by 11 per cent. Appealing to the United States Circuit Court of Appeals, the decision was reversed and an injunction issued. According to a trade journal it is generally conceded in the candy industry "that price ceiling violations are rampant in the candy business."[2]

Regional surveys made in 1942 revealed widespread violation of General Maximum Price Regulation. In region five 70 per cent of the retail stores investigated were reported in violation. In the first quarter of 1943 OPA made a survey of 230 coal-mining communities in the East, the Middle West, and the South, to discover the degree of compliance under three typical food price regulations. "Except in Kentucky, a substantial amount of noncompliance was found with respect to all the commodities covered by the survey." In West Virginia 44 per cent of the items checked under one regulation were being sold at unlawful prices, 38 per cent under another regulation, and 17 per cent under the third. In other states the violations ranged up to 40 per cent. "Moreover the conditions found to exist in the mining communities were duplicated in other communities nearby."[3]

Certain types of price control presented greater difficulties than others. This was particularly true in the apparel industry, where the endless variety of styles and qualities, the seasonal nature of the business, and the large number of producers all created barriers against effective enforcement.[4]

The record of rent control is better than for commodities. In most cases brought to court the defendant either pleaded guilty or was convicted. Fines ranged from $25 to $2,750.[5]

OPA fared well in the courts. In the first four months of 1943 ninety-six per cent of OPA cases were terminated in favor of the government. In 1,496 civil and criminal cases the defendants were successful in only 58. OPA was successful in 98 per cent of its civil cases and in 93 per cent of its criminal cases. Thirty-four out of thirty-five treble damage suits brought by the Administrator against commercial violators were

[1] Office of Price Administration, *Fifth Quarterly Report*, p. 10.
[2] *Business Week*, May 22, 1943, p. 78.
[3] Office of Price Administration, *Fifth Quarterly Report*, p. 57.
[4] Office of Price Administration, *Sixth Quarterly Report*, p. 60.
[5] Office of Price Administration, *Fifth Quarterly Report*, p. 60.

decided in favor of the government. The highest fine involved was $410,219.[1]

The scattered evidence presented in the preceding paragraph is indicative of much more evidence which could be presented. Added together it seems to support the conclusion that if OPA had been given adequate appropriations it could then have engaged adequate personnel and could have enforced the Emergency Price Control Act with a high degree of success. All things considered, those charged with the enforcement of price control have done a reasonably good job; it is not their fault that enforcement activities have not been even more effective.

The Importance of Price Control. In an economy in which the price system is the device which guides and controls all producing and consuming activities the importance of reasonable stability in prices is apparent. In normal times prices are constantly in a state of flux; but while some prices are rising others are falling and the general trend may be a moderate rise and fall. Extreme inflationary increases and extreme deflationary decreases are disturbing if not destructive to the operation of the economy. An inflationary situation very easily gets out of control and then races like a flood, carrying the price system with it at an accelerating pace until its usefulness is practically destroyed. The 1914 dollar which would purchase only 48 cents' worth of goods and services in 1920 meant that the savings, the annuities, the insurance policies of millions of people had been reduced by 52 per cent. Extreme and inequitable losses of that type are demoralizing. This is what is meant by the phrase so frequently repeated that unless we control prices we may win the war abroad but lose it on the home front. Although a few individuals may gain as a result of inflation the vast majority of Americans and the nation as a whole stand to lose irreparably if prices are not controlled. This is a task in which each individual should enlist, performing his functions as a consumer and as a citizen intelligently. This means that as a consumer voter and as a citizen voter he should insist upon adequate price-control legislation and enforcement and should do all he can to secure them.

American citizens have long been accustomed to great freedom in their economic life both as producers and as consumers. All of them chafe under wartime controls and look forward longingly to the days when once more they will be free to produce and to consume as they wish. But price control is even more important in the period of reconversion to a peace economy than it is during the period of conversion from a peace economy to a war economy. If we are reasonably successful

[1] Office of Price Administration, *Fifth Quarterly Report*, p. 65.

in holding the line for the duration of the war much of the gain might be lost if price controls were removed immediately upon the cessation of hostilities. It will probably take one and a half or two years to reconvert our economic system to a peace basis. During that period there will be consumers with $22,500,000,000 or more stored up purchasing power eager to buy the products which have been unavailable in wartime. If allowed to go into the market place without control that flood of purchasing power would result in a tragic rise in prices and a loss of the home-front war.[1]

For the same reasons it will be imperative to maintain consumer credit control. Unless price control and rationing are supplemented with consumer credit control, installment and other forms of credit buying might exert a serious inflationary influence.

Summary

Although our economic system is not organized to fight wars, we find ourselves involved in armed conflicts from time to time. It then becomes necessary to change our goals. The process of converting a peace economy to a war economy involves sweeping changes, including allocation of resources, the freezing of incomes, the control of prices, and the rationing of consumer goods.

Consumer responsibilities are even greater in wartime. The choosing, the purchase, and the use of economic goods require more rational action.

Governmental aids to consumers become more important in wartime. In the period beginning June, 1940, Federal regulatory aids were more important than the positive aids. Probably most important of the regulatory aids was price control, which, up to January, 1944, had passed through six stages. Although price control has been incomplete it has been effective where applied. It has been shown that we know how to control prices and our record would be better if it were not for an inflationary bloc in Congress.

Although Australia placed advertising under control early in the war, the Federal government of the United States has not only not controlled advertising but has encouraged its expansion by permitting firms to treat it as an expense of business before computing profits on which excess profits taxes are based.

If the war on the home front is to be won it is imperative that prices be controlled, not only during the war but also during the period of reconversion.

[1] For an elaboration of the importance of price control see Ferguson, Donald G., and others, *What Will Inflation and Devaluation Mean to You?*, American Institute for Economic Research, Cambridge, Massachusetts.

QUESTIONS FOR DISCUSSION

1. Why are price control and rationing necessary in a war economy?
2. How do the functions and responsibilities of consumers in wartime compare with those of peacetime?
3. Is budgeting more or less helpful in wartime?
4. Is National Service Life Insurance a good buy?
5. How can one hedge against depreciation in the capital value of his life insurance estate?
6. Is it possible to escape higher rents by purchasing a house in wartime?
7. How effective was the program of the Consumer Division?
8. What is selective price control? In what stage was it used? Why was it abandoned?
9. How much did rent control save renters in 1943? Did owners of rental properties lose that much?
10. What wartime controls were placed on installment selling? Why?
11. What did General Maximum Price Regulation provide?
12. Why was rationing of food and shoes started in 1943?
13. Explain the community price ceiling system.
14. Why do farmers favor "controlled inflation"?
15. What are the various forms of price increases?
16. Are standards and grade labeling essential to effective price control?
17. Did the volume of advertising increase or diminish after 1941? What would you expect if you were unaware of the facts?
18. What is the relation between price control, "Little Steel" formula, and subsidies?
19. How does price control in World War II compare with that in World War I as to effectiveness?
20. What was the extent of price control compliance in 1943?
21. Would you advocate removal of price controls immediately after the shooting stops?

PROBLEMS AND PROJECTS

1. Review one of the four books cited on page 631.

2. Outline the consumer protection program you would have supported if you had been appointed Consumer Commissioner in 1940.

3. Gathering your material from various sources, write a report on the 1941 National Conference on Nutrition for Defense.

4. Interview ten or twelve installment credit dealers asking their opinions on these questions:

   a. Was installment credit control necessary?
   b. Did it accomplish its purpose?
   c. Should credit controls be abolished after the war?

Summarize their answers in a report.

5. Go to your nearest rent-control office, or interview a rent-control official, and secure data on rent control in your area; then interview a few selected owners of rental properties and a few renters to discover their opinions on rent control; present your findings in a report.

6. Write a paper on the community price ceiling system, evaluating it in comparison with the General Maximum Price system.

7. Read selected portions of *Brand Names and Newsprint* and write a summary of your findings and your reactions.

8. Write a summary digest of the last two OPA *Quarterly Reports.*

9. Interview the members of your local price panel and write a report describing and evaluating their work.

10. In January, 1944, the New York State Food Merchants Association conducted a survey among its 5,000 members to discover their attitudes toward OPA. The opinion was almost unanimous that retail grocers would be worse off without OPA. (*New York Times*, January 23, 1944, Section 5, p. 1.) Interview 5 or 10 retail grocers in your area and compare their attitudes with those of New York merchants; include your findings in a report.

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